COMMON QUESTIONS ASKED BY FOREIGN PEOPLE ABOUT U.S. TAXES

August 2015 Edition

BARNES & ASSOCIATES CERTIFIED PUBLIC ACCOUNTANTS, P.A.
FORT LAUDERDALE

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The information in this booklet is subject to change without notice. Application of the information to specific circumstances requires the advice of a certified public accountant and/or attorney who must rely upon their own sources of information before providing advice. The information in this booklet is intended only as a general guide and is not to be relied upon as the sole basis for any decision without verification from reliable professional sources familiar with the particular circumstances and the applicable laws in force at that time. If any of the matters described in this booklet are of interest to a particular person, the individual circumstances should be reviewed with a competent certified public accountant and/or attorney familiar with the laws of that individual's present country of tax residence to determine whether the techniques described as useful in dealing with U.S. taxes may have adverse tax consequences in that other country. We and our contacts worldwide would be pleased to assist in this determination.

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COMMON QUESTIONS ASKED BY FOREIGN PEOPLE ABOUT U.S. TAXES

A. HOW ARE FOREIGN PEOPLE (RESIDENT ALIENS, GREEN-CARD HOLDERS, AND NON-RESIDENT ALIENS) TAXED BY THE U.S. ON THEIR INCOME?

Resident aliens are taxed in the U.S. on their **worldwide income**. Worldwide income can include income earned by certain trusts and foreign corporations whether or not actually distributed. This comes as a surprise to many people who come from countries that do not tax foreign income. Many people apply for and receive green cards (permanent resident cards) or stay in the U.S. with or without a visa for over 6 months before they realize that they have thus become taxable in the U.S. on their worldwide income.

Non-resident aliens are taxed by the U.S. only on **certain types of U.S. income. (See Question E for a description of those types of income).**

B. WHAT FACTORS CAUSE A NON-RESIDENT ALIEN TO HAVE RESIDENT ALIEN STATUS FOR TAX PURPOSES? IF A NON-RESIDENT ALIEN IS DEEMED TO BE A RESIDENT ALIEN, THEN WHEN DOES THE RESIDENCY PERIOD BEGIN?

A non-resident alien attains the status of a resident alien for U.S. income tax purposes if the criteria of either of the substantial presence or green-card tests are met. An alien may also be considered a resident alien if the person qualifies and wishes to utilize a special residency election. The substantial presence test and the first-year election are based on the number of days an alien is physically present in the U.S. For the purposes of these tests, there are certain circumstances that exclude days of presence from being counted as well as certain individuals who are exempt from these tests. In conclusion, the starting date of residency is dependent upon the residency test that determines an alien individual to be a resident alien.

B. Continued

1. RESIDENCY TESTS

a. Substantial Presence Test

In the absence of a treaty provision to the contrary or a special status exemption, an individual who spends **183 days or more in the U.S. during the current year is deemed to be a resident alien and is subject to U.S. income tax on their worldwide income.** This substantial presence test is a matter of law and applies even if the individual has a "closer connection" with another foreign country for that year (See Chart B-1).

b. Green-Card Test

An individual who possesses a green card is considered a resident alien regardless of time spent in the U.S. A green-card holder will continue to be considered a resident alien for U.S. income tax purposes as long as the permanent resident card has not been administratively abandoned or revoked. Therefore, an individual who leaves the U.S. for an extended period of time is still considered a resident alien and subject to U.S. income tax on their worldwide income as long as they continue to hold a green card (See Chart B-2).

c. First-Year Residency Election

Individuals who have moved to the U.S. and are present for fewer than 183 days during a current year may elect to be taxed as a resident alien for the year of their move to the U.S. (See Chart B-3). This election may be made if the individual does not qualify under the substantial presence test (See Question B, 1, a thru B, 1, d) or the green-card test (See Question B, 1, b).

To qualify for the first year residency election, an electing individual must:

i. have been a non-resident alien in the year preceding the election year;

ii. not qualify as a resident alien for the election year under the substantial presence test or the permanent residence test;

iii. be present in the U.S. for a period of at least 31 consecutive days in the election year;

iv. be present in the U.S. for 75% of the "testing period;" and

v. qualify as a resident alien under the substantial presence test for the year following the election year.

B Continued

The "testing period" mentioned in Question B, 1, c, iv above is the period that begins with the 1st day of the 31 consecutive days an individual stays in the U.S. and ends on the last day of the election year. Thus, it becomes important for an individual who wishes to utilize this election to have as few days of absence from the U.S. during this period as possible.

It is important to note that for those individuals who are close to meeting the 75% test, up to 5 days of absence from the U.S. will actually be considered as though the person was present in the U.S. in order to meet this test. Also of importance is the fact an individual is not treated as present on any day during which the individual is an "exempt" individual as described in Question B, 2.

The following example illustrates the above information:

Jones, a citizen of foreign country Z, is a non-resident who has never before been a U.S. resident for tax purposes. Jones travels to and from the U.S. as follows:

January 1, 2012 – October 31, 2012 – Country Z
November 1, 2012 – December 1, 2012 – U.S.
December 2, 2012 – December 16, 2012 – Country Z
December 17, 2012 – December 31, 2012 – U.S.

During 2013, Jones is a resident of the U.S. under the substantial presence test. Jones may elect to be treated as a resident of the U.S. for 2012 because:

- he was not a resident for the year preceding the election year;
- he would not qualify as a resident under the green-card or substantial presence tests during the election year;
- he was present in the U.S. in 2012 for a 31 consecutive day period of presence (November 1st through December 1, 2012);
- he was present for at least 75% of the days following (and including) the first day of the 31 consecutive day period of presence (46 total days of presence in the U.S./61 days in the "testing period" from November 1, through December 31 – 75.4%); and
- he was a resident following the election year under the substantial presence test.

d. <u>"Look-Back" Substantial Presence Test</u>

This test applies to individuals whose intermittent presence in the U.S. spans a period of several years. A non-resident alien is deemed to be a resident alien when they are in the U.S. for 31 days or more in a current year and the sum of the number of days they are present during the current year and the two preceding calendar years when multiplied by the applicable multiplier, equals or exceeds 183 days. The applicable multipliers are 1 for the current year, 1/3 for the first preceding year and 1/6 for the second preceding year (See Chart B-1).

B Continued

The following example illustrates the above information:

Harris, a non-resident individual, is present in the U.S. for 122 days during 2012. He was also present in the U.S. for 122 days during 2011 as well as 2010. To determine his status for the current year, Harris computes his days of presence by using the applicable multipliers.

YEAR	DAYS IN U.S.	MULTIPLIER	DAYS PRESENT
2012	122	1	122
2011	122	1/3	40 2/3
2010	122	1/6	20 1/3
			183

Harris is considered to be present in the U.S. for 183 days and meets the substantial presence test. Accordingly, Harris is a resident alien for the current year unless he proves a "closer connection" to another country as described below.

NOTE: Fractional days that result from the use of the multipliers are not rounded up to whole days.

Persons who meet U.S. residency under the "look-back" substantial presence test may avoid U.S. residence status, if they provide proof that they meet a series of facts and circumstances proving a "closer connection" to another country. An alien individual who changes his tax residence between two foreign countries can have a **"closer connection" to two foreign countries (but no more than two) during the calendar year**.

There are three elements that must be satisfied in order to qualify for the "closer connection" test. A person:

- must be in the U.S. less than 183 days in the current year (which is why individuals under Question B, 1, a do not qualify);
- must have a tax home in another country other than the U.S. as well as a "closer connection" and be subject to tax as a resident in such country(s); and
- must comply, on a timely basis, with certain reporting requirements (Form 8840).

For purposes of the second requirement above, a tax home is defined as the regular or principal location of business. If the person is not engaged in any sort of business, then the regular place of abode is considered. A "closer connection" is established if the person has maintained more significant contacts with the foreign country than with the U.S. The following facts and circumstances are used to examine if more significant contact has been maintained with a foreign country:

- the location of the individual's permanent home;
- the location of the individual's family;
- the location of personal belongings, such as automobile, furniture, etc.;
- the location of social, political, cultural or religious organizations in which the individual has a current relationship;
- the location of the individual's personal bank account;
- the type of driver's license held by the individual;
- the country of residence designated by the individual on forms and documents;
- the types of official forms and documents filed by the individual;
- where the individual votes; and
- the location where the individual conducts business activities (other than those that constitute his tax home). An individual's tax home will be considered to be his regular place of abode if he is not engaged in a trade or business.

As previously mentioned, the above factors apply to determine with which countries a "closer connection" lies. Individuals who are considered U.S. tax residents under the traditional substantial presence test (Question B, 1, a) or green-card test (B, 1, b) are disallowed from using the "closer connection" exception and are automatically resident aliens.

All other individuals who do not meet any of the residency tests outlined above are considered non-resident aliens for U.S. income tax purposes.

2. DAYS OF PRESENCE

A day is counted as a day of U.S. presence for the above residence tests if the individual is physically present in the U.S. at any time during that day. Therefore, presence for part of a day, such as the day of arrival or departure from the U.S., counts as a full day. However, there are certain types of U.S. presence that are disregarded in determining residency for U.S. income tax purposes. They are the following:

- days that an individual is prevented from leaving the U.S. because of a medical condition **that arose while in the U.S.;**
- days that an individual is in transit between two points outside the U.S.;
- days on which a regular commuter residing in Canada or Mexico commutes to and from employment in the U.S.;
- certain crew members of foreign vessels that are engaged in international transportation services. Days of presence under Internal Revenue Service Code Section 861(a)(3) are not considered as days of presence under the substantial presence test; and
- days in the U.S. as an "exempt" individual, such as a foreign diplomat, teacher or trainee, student, or professional athlete in the U.S. to compete in a charitable sports event. The members of the immediate families of exempt individuals (except for the professional athlete exemption) also are exempted from the days of presence computation during the same period as the "exempt" individual.

B Continued

Achieving status as an "exempt" individual for the most part is difficult, with the exception of the student visa. Requirements for this visa include full-time student status in the U.S. normally for a period not to exceed five years along with very limited work eligibility. Individuals wishing to apply for exemption status as a student are required to timely file Form 8843. Failure to timely file the form can result in an individual losing the right to the "exempt" days otherwise allowable under the tax law.

3. RESIDENCY STARTING DATES

The starting date of a person's residency depends on how the residency status was achieved. Individuals who are admitted as **lawful permanent residents** ("green-card holders") begin their residency upon arrival in the U.S. with a green card.

Individuals who meet the substantial presence test, generally begin their residency the first day physically present in the U.S. The 10-day "de minimum exception" overrides this general rule and was enacted to avoid penalizing individuals who made brief business trips or house hunting trips prior to their move. The exception provides for up to 10 days of presence to be disregarded for purposes of determining the start of U.S. residency only. As an example, an individual who visits the U.S. for 7 days in January and then moves to the U.S. on May 15, will be a resident alien for that year, but the starting date will be May 15. **Notwithstanding the exclusion, the days count for purposes of counting total days present in the U.S.**

Individuals who elect to be treated as resident aliens begin their residency on the 1st day of the 31 consecutive day period while in the U.S.

Chart B-1

SUBSTANTIAL PRESENCE TEST
For Individual From Non-Treaty Country

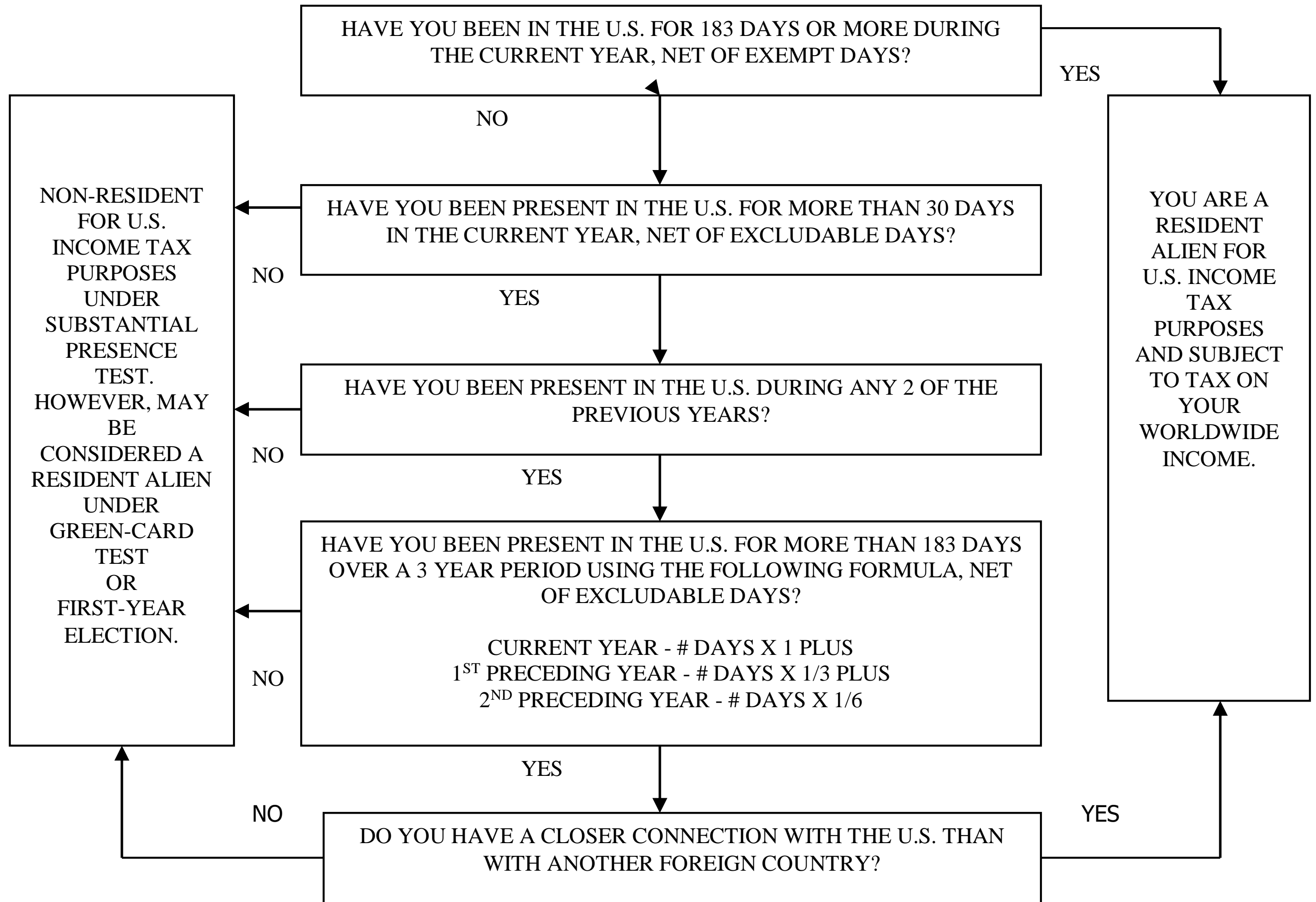


CHART B-2

GREEN-CARD TEST
(PERMANENT RESIDENCE)

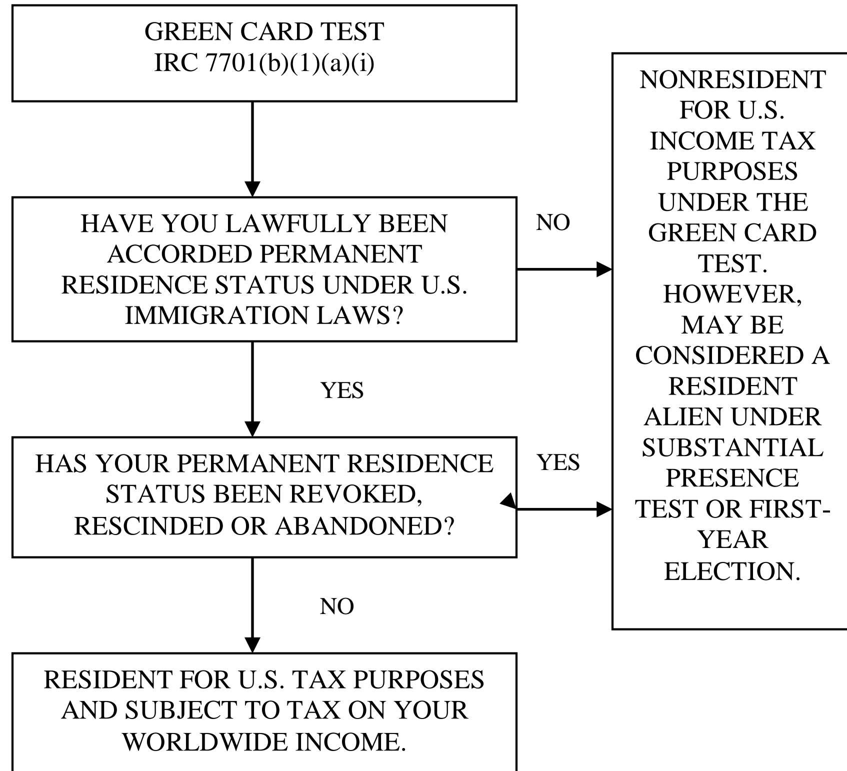
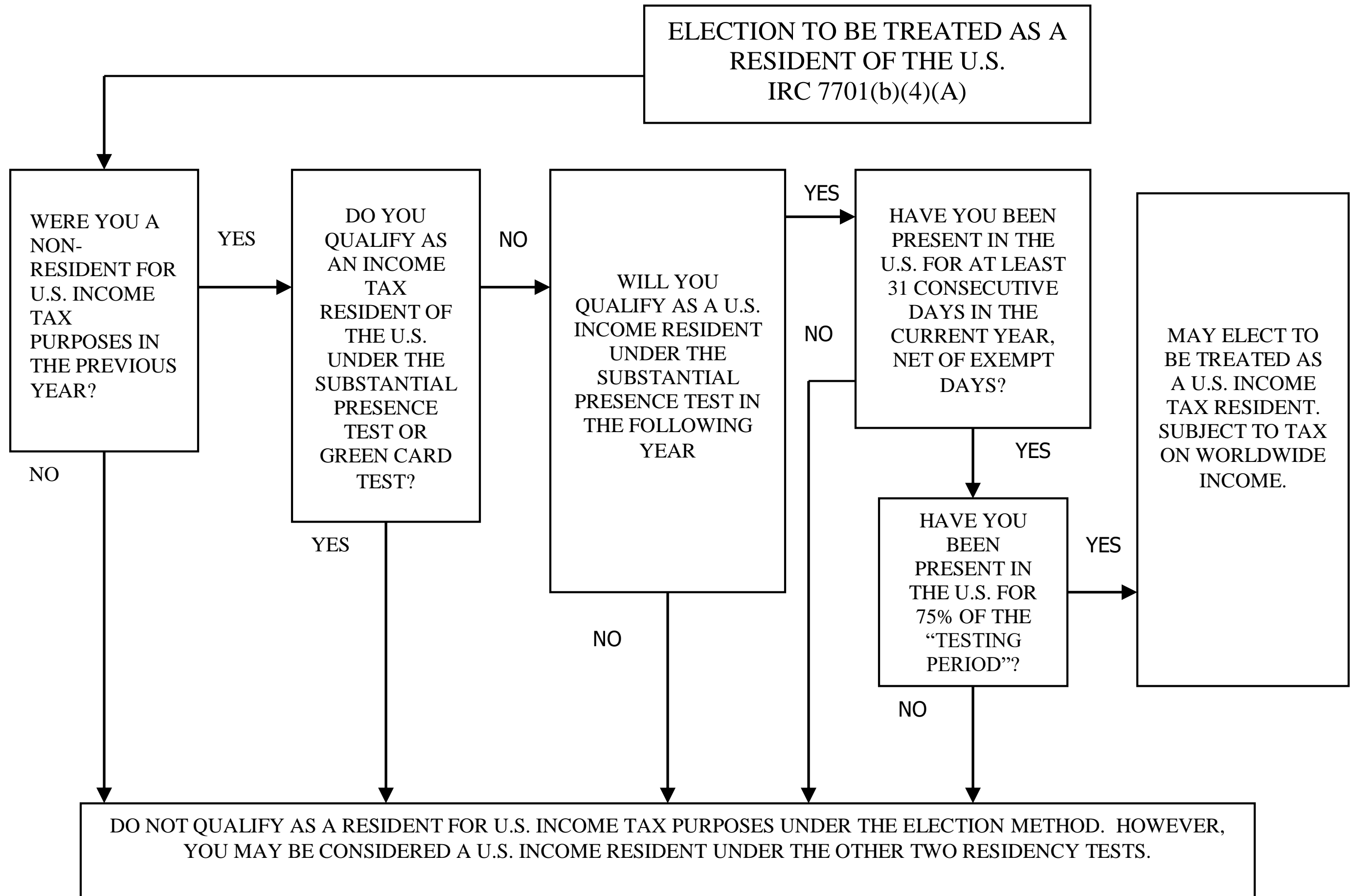


CHART B-3

WHEN NON-RESIDENT INDIVIDUALS BECOME RESIDENTS FOR U.S. TAX PURPOSES ELECTING TO BE TREATED AS A RESIDENT (TEST 3 OF 3)



C. HOW CAN A U.S. RESIDENT TERMINATE HIS/HER U.S. RESIDENCY STATUS? HOW DOES THE U.S. TAX HIS SUBSEQUENT INCOME?

1. TERMINATION OF U.S. RESIDENCY

The means available for terminating residency depends upon individual circumstances.

A. Residents who were treated as U.S. tax residents in prior year(s) based solely upon physical presence (See Question B, 1, a and Question B, 1, d) who have no green card and have made no first-year election to be taxed as a resident.

1) If treaty is applicable to circumstances in "departure year," avoid U.S. tax residency by electing, under treaty, to be taxed as a resident of the treaty country for the portion of the year one qualifies as a resident of the treaty country by filing Form 8833; or
2) Avoid residency effective January 1, by spending fewer than 30 days in U.S. in "departure year;" or
3) If more than 30 days are spent in the U.S. in "departure year," avoid residency effective January 1, by spending fewer days in the U.S. in the departure year than the number of days in U.S. which would cause the computed total number of days under the "look-back" rule described in B, 1, d not to exceed 182; or
4) If total days in the U.S. under the "look-back" rule exceeds 182 days, but total days in the U.S. in the departure year is less than 183, then it is necessary to establish that there is a "closer connection" to another country (or up to two other countries) during the "departure year." Such qualifications would terminate residency under these circumstances, effective January 1; or
5) If "4" above is an uncertain result as to the "closer connection" test or if present in the U.S. in "departure year" for more than 182 days in the departure year, a resident alien can end the year effective at any point during the year by filing Form 1040C and immediately establishing residency and a closer connection in a country other than the U.S. Form 1040C must be filed to document such departure within two weeks of departure. The Form 1040C is filed, in person, at an Internal Revenue Service office. Such departing residents are taxed as if they had two separate tax years; one as a resident and one as a non-resident.

B. Residents who were treated as tax residents of the U.S. in prior year based on first-year election (See Question B, 1, c):

1) Must spend the next year as income tax residents of U.S.;
2) After that, terms of Question C, 1 above apply.

C. Residency based upon possession of a green card (See Question B, 1, b) continues until revoked or administratively or judicially determined to have been abandoned. Presumably green-card residency status continues even if the cardholder does not spend a single day in the U.S. in a given calendar year. A person turning in a green card should proceed under the guidelines described in Question C, 1 above.

Once the alien has been a resident for at least 183 days for each of three calendar years (but fewer than 8 years as a green-card holder) and then departs and becomes a non-resident alien, the status of non-resident alien must be maintained for 3 years or the alien becomes retroactively taxable by the U.S. on U.S. source income and possibly tax ed on the same income as that of a U.S. citizen or resident who is deemed to have expatriated for tax avoidance reasons (discussed below).

2. U.S. EXPATRIATION RULES

The Heroes Earnings Assistance and Relief Tax ("HEART") Act of 2008 revised the expatriation rules for U.S. citizens and long-term permanent residents (individuals who have held a green card for at least 8 out of the 15 immediate tax years preceding relinquishment) who expatriate after June 16, 2008. Previous standards required that a determination be made if an individual expatriated for tax avoidance purposes. Under the new HEART standards, no tax avoidance motive is required. Individuals meeting one of the three tests, described below, for covered expatriates are subject to a departure tax on all assets. A "mark-to-market" valuation of assets is made as of the day prior to expatriation and all unrealized gains and losses are deemed to be realized. These "deemed realized" gains are then added to the income tax return of individual, in the amount that exceeds $680,000 in 2014 and $690,000 in 2015.

Three categories of assets are exempt from HEART departure tax.

1. Deferred compensation, including pension plans and annuities
2. Tax deferred accounts, including individual retirement accounts, health savings accounts, Coverdell education and qualified tuition accounts
3. Non-grantor trust assets (Note: **Grantor** trust assets are **not** excluded and are subject to "mark-to-market" valuation.)

These assets are excluded from the departure tax because they will be paid to a nonresident of the US (individual's status after expatriation) and therefore subject to 30% withholding at the time of payment.

An individual is presumed to be a "covered expatriate" and is subject to departure tax on assets if the individual either:

1. for calendar year 2014, has an average annual net income tax liability for the five preceding years that exceeds $157,00 in 2014 and $160,000 in 2015 (adjusted for inflation);
2. has a net worth as of the date of expatriation of $2,000,000 or more; or
3. fails to certify under penalties of perjury that he or she complied with all U.S. federal tax obligations for the preceding five years and provides any evidence of compliance required by the Treasury Department.

C Continued

Exceptions to the applicability of the departure tax are available to dual citizens and minors who have had no substantial contact with the U.S. under limited circumstances. These individuals can avoid being subject to the departure tax if they have complied with the US tax filing requirements prior to the date of expatriation.

A U.S. citizen or long-term permanent resident, whether or not subject to the departure tax, will continue to be taxable as a U.S. citizen or resident until notice is given to the Secretary of State (in the case of a former U.S. citizen) or the Secretary of Homeland Security (in the case of a former U.S. long-term permanent resident) and submits Form 8854 (Expatriation Initial Information Statement). Failure to file could result in a penalty of $10,000.

An example of how the departure tax is determined – Paula, a single US citizen, owns a home worth $3,000,000, securities portfolio worth $1,500,000 and cash of $250,000 on the day before she relinquishes her citizenship. She originally purchased her home for $1,050,000 and her securities portfolio was inherited at a value of $2,400,000. Paula's average annual net income tax for the preceding 5 years is greater than $155,000 and she has complied with all US tax filing requirements for that period.

Asset Value on Date Immediately Prior to Date of Expatriation	Basis	Gain(Loss)
Home: $3,000,000	$1,050,000	$1,950,000
Securities: $1,500,000	$2,400,000	($900,000)
Cash: $ 250,000	$ 250,000	-0-
Total: $4,750,000	$3,700,000	$1,050,000

Paula has a deemed capital gain on the "sale" of her home of $1,950,000. She is not entitled to the $250,000 exemption against the gain on the sale of a primary residence that is normally allowed to US citizens and residents.

She is allowed to offset the deemed capital loss on the "sale" of her securities portfolio. Realized losses under the departure tax regime are recognized using current US tax laws. If Paula had no capital income to offset her capital loss, she would only be allowed to use $3,000 against her deemed income; the standard amount used for excess capital losses.

Paula's net deemed realized gain is $1,050,000. $382,000, the amount in excess of $668,000, would be included as additional taxable income on her 2013 US income tax return.

The gains realized under the “mark-to-market” asset valuation do not result in any cash flow to the individual, potentially creating a scenario in which tax is due on phantom income and no cash is available to pay the tax debt. Individuals unable to pay the tax at the time of expatriation may elect to pay the tax as the assets are sold. Security in the form of a bond or letter of credit must be posted. Tax will be due by April 15th of the year following the year in which the taxable asset is sold. In the event that an individual dies before the assets are sold, tax will be due with the individual’s final income tax return. Interest is charged on the unpaid tax and accrued from the date of expatriation at the applicable federal rate for underpaid tax of an individual.

The expatriation rules also affect the U.S. estate and gift tax treatment of individuals subject to departure tax. Gifts and bequests to U.S. persons from nonresidents are generally not subject to tax in the U.S. In order to avoid expatriates’ assets from escaping U.S. estate and gift tax, the HEART Act added new provisions applicable to U.S persons receiving gifts or bequests from covered expatriates.

Tax is assessed on the expatriate’s gift or bequest at the highest estate or gift tax rate for the year. The liability for remitting the tax due now lies with the U.S. recipient of the gift or bequest. If the covered expatriate files a gift or estate tax return and pays the tax due, there is no further liability to the U.S. recipient. The $14,000 annual exclusion is allowed for gifts from covered expatriates.

D. HOW IS A PERSON WITH DUAL RESIDENCY TAXED?

If an individual has dual-residency status (i.e., a person is treated as a resident under the tax laws of the U.S. and another country), **absent treaty protection**, the individual may be taxed as a resident in both countries. The only relief from double taxation would be the foreign tax credit (See Question J).

Most treaties provide a “tie-breaker” test which contains a series of steps to establish the country of tax residency if dual-residency status arises. The steps are applied sequentially, meaning if the taxpayer’s country of residence can be determined after applying the first step, then no further analysis is required. If the next step is not determinative, then the taxpayer applies the following step of the test until a determination can be made. If after reviewing all the steps a determination cannot be made, some treaties allow for a tie-breaking election by the individual while some treaties leave it to the governments to determine.

D Continued

The tax treaties the U.S. has with Canada, Germany, and France, for example, utilize the following "tie-breaker" tests to determine the country of tax residency for individuals:

- an individual will be deemed to be a resident of the country in which the individual has a **permanent home** available to them; if a permanent home is available to the individual in both countries in question, the individual is considered a resident of the country with which their **personal and economic relations** are closer (center of vital interests);

- if the country in which the individual has their center of vital interests cannot be determined, or if there is not a permanent home available to the individual in either country, the individual shall be deemed to be a resident of the country in which they have an **habitual abode**;

- if the individual has an habitual abode in both countries or in neither of them, the individual shall be deemed to be a resident of the country of which the individual is a **national***;

- if the individual is a national of both countries or of neither of them, the competent authorities of both countries will **settle the question by mutual agreement.** Treaties with certain countries (including Germany) now have provisions to settle un-agreed cases by mandatory binding arbitration.

  *The U.S. tax treaty with Canada uses the term "citizen" for this tie-breaking provision.

A person who would otherwise be considered a resident of the U.S. for income tax purposes, but relies on a treaty to be taxed as a resident of another country, must file Form 1040NR along with Form 8833 to disclose this position. Question Q lists the income tax treaties between the U.S. and various foreign countries as well as information on making treaty elections.

According to U.S. treasury regulations, the affect a "tie-breaker" election has on an eligible taxpayer is for this individual to be considered a non-resident alien for all purposes of the Internal Revenue Code in calculating his/her own U.S. tax liability with a few exceptions. One of these exceptions includes preserving U.S. resident alien status to determine whether a foreign corporation is considered a "controlled foreign corporation" which is discussed in Question M, 5, a.

Use of an income tax treaty may exempt non-real estate capital gains realized by a foreign individual who is present in the U.S. for 183 days or more from being subject to U.S. income tax on such capital gains. Otherwise, most foreign persons in the U.S. for 183 days or more are subject to capital gains taxes on U.S. assets even if their status is regarded as a non-resident for income tax purposes (See Question E, 1, a).

D Continued

If a treaty thus applies, the election is allowed even though the individual has a green card or is in the U.S. for more than 183 days. Note: U.S. immigration problems may result from this election. Specifically, if a green card holder applies for U.S. citizenship (generally allowed after five years as a green card holder) they must comply with the requirement that they file as a U.S. tax resident for each year they were a green card holder. Having elected under a treaty to be treated as a tax resident of another country can deny qualification for U.S. citizenship. Amended returns <u>may</u> solve this problem.

E. WHICH U.S. SOURCES OF A NON-RESIDENT ALIEN'S INCOME ARE TAXED BY THE U.S. AND WHICH ARE EXEMPT?

1. <u>INCOME EXEMPT FROM U.S. TAX IF NOT EFFECTIVELY CONNECTED WITH CONDUCT OF U.S. TRADE OR BUSINESS</u>

The following information assumes that a properly completed Form W-8BEN has been completed and submitted to the U.S. payor. Failure to file this form would subject all proceeds to federal withholding at a 30% rate. (See Question G, 1).

a. Capital gains from U.S. sources other than U.S. "real property interests" (if alien is non-resident for income tax purposes). **However, Congress may limit or remove this exemption in future tax legislation. NOTE: The capital gains of a non-resident may be subject to U.S. taxes in the limited instances (e.g., diplomats or students) that the individual is present in the U.S. for more than 183 days but is still considered a non-resident.**

b. Interest earned on U.S. bank deposits, certain U.S. savings and loan associations, and insurance companies. NOTE: In August of 2002, the Internal Revenue Service proposed tax regulations which would require that financial institutions report to the department, on an annual basis, payments of all U.S. bank deposit interest to certain non-residents of the U.S. Individuals from Australia, Denmark, Finland, France, Germany, Greece, Ireland, Italy, the Netherlands, New Zealand, Norway, Portugal, Spain, Sweden and the UK would all be subject to this reporting. The proposed regulation is currently facing strong opposition by many in the financial community as unnecessary for the enforcement of U.S. tax laws and discouraging foreign investment. Canadians are currently the only individuals subject to this interest reporting under current tax law. We have no further information on this proposed regulation at this time.

c. "Portfolio Interest" paid to a non-resident individual or foreign corporation through the issuance of a "registered" debt instrument. An obligation is in registered form if both the principal and any stated interest are transferable by (1) surrendering the instrument for re-issuance or issuance of a new instrument to the transferee, or (2) rights to principal and stated interest can be transferred only through a book-entry system maintained by the issuer or agent. Additionally, certain reporting requirements must be met to confirm the recipient's status as a foreign individual. Interest will not qualify as "portfolio interest" regardless of meeting the requirements above if:

- paid to a 10% shareholder or partner of the borrower
- received by a "Controlled Foreign Corporation ("CFC") from a related person;
- paid as certain contingent interest
- paid as certain bank interest; or
- the lender is involved in back-to-back financing and is either unable or unwilling to provide proof that the ultimate beneficial owner of the funding source is an unrelated party

d. Dividends from certain U.S. corporations engaged in foreign business.

e. Income specifically exempted by treaty.

f. Compensation for services performed for a U.S. business outside the U.S.

g. Compensation for services in the U.S. if such compensation is less than $3,000, and if present not more than 90 days in the U.S. as an employee or under contract with a foreign business. (Different rules may apply if a treaty is in force.)

h. Income attributable to a U.S. non-resident spouse in a "mixed" marriage (one spouse considered a U.S. non-resident while the other is subject to U.S. income tax as a resident) assuming they do not own community property.

i. Other exempt income described in Question H.

2. <u>INCOME TAXABLE BY U.S.</u>

a. All income from U.S. sources effectively connected with a U.S. trade or business (See Question G, 1, b for the importance of filing Form W-8ECI). Effectively connected income also includes a partnership interest in a U.S. trade or business, most investments in U.S. extractive industries, the operation of U.S. "real property interests," and the maintenance of a U.S. business office in regard to sales within the U.S.

b. All U.S. source interest, dividends, rents and royalties not specifically exempted.

c. All U.S. compensation for services not specifically exempted.

d. Capital gains from the sale of a U.S. “real property interest.” The sale of a U.S. “real property interest” includes the sale of the shares or liquidation of a U.S. corporation by a foreign owner if the corporation’s assets consisted of 50% or more of U.S. real property at any time during the 5 years preceding the sale. However, if all such real property assets were sold in transactions taxable to the corporation, then such assets are disregarded in this test and the sale or liquidation of the corporation is not a taxable event. This definition includes foreign corporations that have elected to be taxed as a U.S. domestic corporation under Internal Revenue Code (IRC) 897(i).

   However, the sale of the shares of a foreign corporation holding U.S. real property is not deemed to be the sale of a U.S. real property interest. Therefore, no tax is required to be withheld at the time of the sale of such foreign corporation shares. Unfortunately, upon the ultimate sale of the actual real estate by the corporation, capital gain tax will become due on the gain attributable to the entire period the property is held by the foreign corporation.

F. WHAT IS THE DIFFERENCE BETWEEN RESIDENT ALIENS VS NON-RESIDENT ALIENS AND DOMICILIARY VS. NON-DOMICILIARY ALIENS? HOW DO U.S. ESTATE AND GIFT TAXES AFFECT DOMICILIARY AND NON-DOMICILIARY ALIENS?

1. INTRODUCTION TO THE U.S. ESTATE TAX AS IT APPLIES TO DOMICILIARIES AND NON-DOMICILIARIES

The U.S. estate and gift tax has always and **will continue to affect domestic and foreign individuals very differently**. Accordingly, we made a distinction between U.S. domiciliary aliens and non-domiciliary aliens as well as resident aliens and non-resident aliens in the following sections. It will become apparent after reading the information that follows that this distinction results in very stark contracts between U.S. estate tax and gift tax treatment.

2. RESIDENT ALIENS VS. NON-RESIDENT ALIENS AND DOMICILIARY VS. NON-DOMICILIARY ALIENS

Different tests exist to determine residency for U.S. income tax purposes and for U.S. estate and gift taxes. The distinction between the terms resident aliens and non-resident aliens is made in order to determine the tax liability of an individual for **purposes of U.S. income taxes**. The terms domiciliary alien and non-domiciliary alien are utilized to determine an individual's tax liability for **U.S. estate and gift tax purposes**. It is important to note that the residency tests for U.S. income tax purposes are much more clear-cut than the "domicile" tests for estate and gift tax purposes which are discussed in more detail below.

For U.S. estate and gift tax purposes, two requirements must be met to be a U.S. domiciliary alien: (1) physical presence in the U.S., and (2) current intent to make a home and remain in the U.S. indefinitely must coincide to establish domicile. Once these factors coincide, domicile is established in the U.S. until these factors coincide elsewhere.

Since the estate and gift tax definition of domicile hinges on intent, **it is possible for an individual to be a U.S. tax resident, but still not have established U.S. domicile for estate and gift tax purposes and vice versa** (it would be difficult for a green-card holder to prove non-U.S. domiciliary status since they are lawful "**permanent**" residents of the U.S.).

F Continued

In order to determine **intent**, an analysis of facts and circumstances of the individual needs to be considered along with the following factors:

- time in the U.S., both the relative amount of time spent in the U.S. and other countries, and the frequency and duration of travel by the individual;
- location of family and close friends;
- location of primary service providers such as doctors, bankers, and financial advisors;
- mailing address for remittance of dividends, interest, alimony, and other payments;
- location of business interests;
- jurisdiction where returns filed and income taxes paid;
- representations to the public such as the address, telephone and fax numbers on stationary and business cards;
- statements to the public in general will also be considered;
- reference in filed Last Will and Testament to country of domicile;
- existence of a return airplane ticket.

3. U.S. ESTATE AND GIFT TAXES OF U.S. DOMICILIARY ALIENS AND U.S. CITIZENS

a. U.S. Estate Tax of the U.S. Citizen and Domiciliary Alien

The U.S. provides for the transfer of some assets without the payment of gift or estate taxes by means of the "unified credit." The "applicable credit" (formerly know as "unified credit") is a lifetime amount, **applied first to taxable gifts in the limited amount available of $5,250,000 for lifetime gifts**, with any remaining credit applied against estate taxes. **The effective estate tax exemption amounts for bequests by estates of domiciliary aliens and U.S. citizens to persons other than U.S. citizen spouses for** $5,240,000 in 2014 and $5,430,000 in 2015.

Assets includible in the estate of a domiciliary alien can include the spouse's interest in community property if the property was acquired during marriage while domiciled in a community property jurisdiction. Generally, this property retains its nature as community property even if a married couple later immigrates to a non-community property jurisdiction. However, the community property rules of the particular jurisdiction of the couple should be examined as there is little uniformity in the various community property regimes and, therefore, classification as well as treatment of community property will differ. Community property jurisdictions within the U.S. include: Alaska, Arizona, California, Idaho, Louisiana, Nevada, New Mexico, Texas, Washington, and Wisconsin.

b. Enforcement of the U.S. Estate Tax

The U.S. enforces the estate tax through use of a "special estate tax lien" which automatically comes into existence on the date of death of a decedent. It continues for ten years unless, before the end of the ten-year period, the estate tax is paid in full or becomes unenforceable by expiration of the Statute of Limitations for collections. No formal notice of lien is required. Property passing at death is normally dealt with by probate and estate tax proceedings and effectively serves as notice.

The special estate tax lien attaches to the property includable in the gross estate of the decedent. Therefore, where probate property is sold by an estate owing estate tax, the purchaser has bought property encumbered by the special lien and could, therefore, be held liable for unpaid U.S. estate tax. Careful practitioners representing buyers take such precautions as asking the estate representative for evidence that all estate taxes have been paid, seeking the discharge of the special estate tax lien on the property being purchased, and securing indemnity from the estate, should any estate tax liability arise.

There are special measures that can be taken by an estate that wishes to sell U.S. real property but has not received a discharge from the lien where a potential purchaser can be released from any potential U.S. estate tax liability to preserve any contemplated deal.

c. Gift Taxes for Gifts by U.S. Citizens & Domiciliary Aliens

In addition to the "unified credit" exemption described before, U.S. citizen and domiciliary alien donors of gifts are entitled to an annual exclusion amount of $14,000 per recipient (donee) per year for non-spousal recipients. This annual exclusion amount, which is adjusted for cost of living, can be maximized by electing to "split gifts" with a spouse to increase the exclusion amount to $28,000 per donee per year. (Also see Table F-1 which describes further exemptions for gifts to spouses.) To be eligible to "split gifts," both spouses must either be U.S. citizens or U.S. domiciliary aliens.

4. U.S. ESTATE AND GIFT TAXES OF THE NON-DOMICILIARY ALIEN

As mentioned in the introduction to Question F, there are disparities in the estate tax treatment of U.S. non-domiciliary aliens versus U.S. domiciliary aliens. The most glaring of these disparities is the availability of the "unified credit" amount and the availability of the unlimited spousal exemption. Unlike U.S. domiciliary aliens who are entitled to the current "unified credit" amount of $5,340,000, U.S. non-domiciliary aliens are still only entitled to the $60,000 "unified credit exemption" amount for the value of U.S. assets. Moreover, non-citizen spouse beneficiaries of the U.S. estates are not entitled to benefit from the unlimited spousal exemption allowed to U.S. citizens. This exemption is only available if the surviving spouse is a U.S. citizen. As mentioned below, a tax planning opportunity does exist if the assets of a non-domiciliary alien are transferred to a "qualified domestic trust," though this provides on a **deferral** of the tax.

Therefore, unless there is treaty protection available, a person who is classified as a non-domiciliary alien, whether or not he is a U.S. resident for income tax purposes, is subject to U.S. estate (death) taxes on all his "U.S. property" in excess of $60,000 which does not pass to a U.S. citizen spouse or to a special trust sanctioned by the 1988 Tax Act called a "qualified domestic trust" and is discussed later.

Canadians and nationals domiciled in countries that have estate tax treaties with the U.S. enjoy special tax provisions that can modify the rules previously described. The Canadian provisions, curiously, are in the income tax convention. Any national from these countries should read their applicable tax convention in applying the rate of tax, exemptions and deductions to determine the applicability of these rules to their estates. Some treaty benefits are discussed at the end of the next section below.

a. U.S. Estate Tax of a Non-Domiciliary Alien

It may come as a surprise to many foreign individuals that they can be subject to the U.S. estate (death) tax. This can occur if the U.S. non-domiciliary alien dies while owning U.S. property which exceeds $60,000 in value.

Examples of U.S. property include, but are not limited to:

- Shares of a U.S. corporation;
- All U.S. real property holdings;
- U.S. personal property including short-term U.S. Treasury obligations; and
- Debt of a U.S. corporation or other U.S. person to a foreign individual.

F Continued

All of these items are generally includable in the taxable estate of a non-domiciliary alien unless specifically excluded by statute.

The tax laws allow for some specific exemptions of property from being subject to the U.S. estate tax. Some specific exemptions are:

- Deposits in U.S. banks (however, if the income of the account is taxable to the alien, the deposits may be includible in the estate).
- Shares of foreign corporations. Note that shares of a foreign corporation are by definition not "U.S. property" and are thus excludable from the estate even if the entity owns U.S. assets.
- Life insurance proceeds on the life of a non-domiciliary alien decedent are excluded from the gross U.S. estate.
- Life insurance proceeds on the life of a U.S. domiciliary alien can be excluded from their estate if the policy is owned by someone other than the insured decedent, including a non-domiciliary alien or a qualified life insurance trust.
- U.S. Treasury Notes and other debt obligations may be eligible for exclusion if certain conditions are met to qualify the debt obligation for the "Portfolio Interest Exemption" detailed in Question E. In general, debt obligations producing income that qualifies for exemption from income tax under the "Portfolio Interest Exemption" provided by IRC Section 871(h) will also be eligible for exclusion from the estate of a non-domiciliary alien decedent. U.S. Treasury and other short-term obligations (183 days or less) that are exempt from income under IRC Section 871(g) as being excluded from definition as original issue discount, would not qualify from exclusion from the estate of a non-domiciliary alien decedent.
- If a decedent held property jointly with a non-U.S. citizen spouse, 100% of the property is included in the taxable estate. However, there is the possibility to limit the U.S. property includible in the decedent's U.S. estate to the portion contributed by the decedent to the purchase of the property. The "consideration-furnished" rules allow for a decedent's estate to exclude from the taxable estate assets for which the decedent did not contribute consideration. Of great importance is evidentiary proof if this position is to be taken such as demonstrating the flow of funds from separately maintained bank accounts. Prior gifts of U.S. property from the survivor to the decedent do not count as "consideration" furnished by the decedent. Community property rules must also be considered.

- Similar to an estate of a U.S. citizen, the estate of a non-domicile may be entitled to a credit for all or part of the estate tax paid with respect to a transfer of property to the decedent by another person. Unlike estates of U.S. citizens where the credit will vary depending on the time that has elapsed between the decedent's death and that of the transferor of property, a surviving spouse who is a U.S. non-domicile is entitled to a credit for previous estate taxes paid. Generally, no credit is allowed if more than 10 years have passed since the transferor's death. However, for surviving spouses who are U.S. non-domiciles, a credit is allowed regardless of how much time has lapsed from when the transferor spouse died. Note that for U.S. non-domiciles, the credit is claimed by surviving spouses only.

Note: Bank accounts and portfolio interest bonds may lose their foreign situs if an individual is considered a non-domiciliary alien of the U.S. but is treated as a U.S. income tax resident. Accordingly, it may be prudent to maintain larger accounts outside the U.S.

There are certain planning opportunities to either defer or reduce the U.S. estate tax. As previously mentioned, U.S. assets that do not pass from a non-domiciliary alien to a U.S. citizen spouse would be subject to U.S. estate tax if the value exceeds $60,000.

A technique to reduce exposure to U.S. estate taxes would be **to encumber U.S. property with debt to reduce the value includible in the estate**. It is very important to be aware that **U.S. debt other than non-recourse debt, (even mortgage debt encumbering U.S. property) does not directly reduce the U.S. taxable estate for a non-domiciliary alien except as provided in a few treaties**. All debt other than non-recourse debt is prorated among all worldwide assets of a non-domiciliary alien decedent. However, care should be taken. The debt obligation would be includible in the U.S. estate of the non-domiciliary holder upon death. However, if the maker of the obligation is a foreign person or entity not a U.S. resident or domestic entity, the obligation is not includible in the estate of the holder. Thus, a sale of the property before death of a non-domiciliary alien to a non U.S. person or entity for a note obligation could serve to eliminate the asset from the U.S. estate of the seller, even if backed by a mortgage on the U.S. property.

Life insurance is widely recommended to fund estate tax requirements where there will be exposure to the U.S. estate tax. Life insurance policies on husband and wife with payment to be made at the death of the **second to die** can minimize premium cost and provide liquidity at the appropriate time when used in conjunction with a "qualified domestic trust" which can defer estate taxes otherwise due at the first death. Life insurance proceeds are exempt from income tax and they can be excluded from the estate tax under the previously described conditions.

A "**qualified domestic trust**" is an elective planning tool that will allow a marital deduction on the first death, but imposes taxation on the second death or earlier disposition by the trust. **This "Q-DOT" trust is a key planning tool used to defer the payment of U.S. estate taxes for resident and non-domiciliary aliens.** It can be created at any time before the estate tax return (Form 706-NA) is filed.

The estate of a foreign domiciliary from a non-treaty country, such as **Mexico**, can report the worldwide estate tax expenses and claim a prorated amount to reduce the U.S. taxable estate. Although this may reduce the U.S. estate tax liability for the estate, the executor to the estate may opt to not take advantage of this benefit. To claim such expenses, the worldwide estate must be disclosed on the U.S. estate tax filing.

See Question M for further discussion on how to reduce exposure to U.S. non-domiciliary alien estate taxes as well as Question O on how to hold U.S. real property with the estate tax in mind.

Treaty provisions can modify or override some the general estate tax rules above which can effectively reduce or eliminate U.S. estate tax exposure. For instance, some allow for the "domicile" rules described above to be overridden. Other treaties reduce the taxable assets transferred to a non-resident effectively providing for a marital deduction. Therefore, it is important to review the tax treaties thoroughly for effective estate tax planning.

Canada is an example of how domiciliaries of the country can benefit from treaty benefits. Although there is no estate convention with Canada and the U.S., the income tax convention between the two countries was modified to include provisions addressing the U.S. estate tax. For instance, the income tax treaty with Canada (which has no estate tax of its own) allows for a **pro-rated unified credit** rather than being limited to the $60,000 generally available to U.S. non-domiciliaries who die owning U.S. property. Other countries with similar provisions (as to the proration of the unified credit available to U.S. citizens) within their estate tax treaties with the U.S. are **Australia, Finland, Germany, Greece, Italy, Japan, Norway and Switzerland.**

The amount of the treaty credit is the unified credit available to a U.S. citizen's estate multiplied by a fraction. The numerator of the fraction is the value of the estate's taxable U.S. assets with the denominator equaling the value of the worldwide gross estate. It is important to note that many estate executors prefer to forego implementing the treaty benefits because, to do so, requires extensive information on the decedent's worldwide assets and information on the estate filings in the decedent's country of domicile.

Some other provisions of interest available to **Canadian domiciles** under the convention include the ability of the executor to claim a credit for the Canadian federal and provincial deemed transfer tax on assets situated outside the U.S. Also available is the ability to exempt from U.S. estate taxation most U.S. property, except U.S. real estate if the estate is considered a "small estate" under the convention. Additionally, a partial exclusion of property passing from the deceased U.S. non-domicile to the surviving U.S. non-domicile is available. The allowance of a **partial marital deduction** or exclusion is also available for domiciliaries of **France, Germany, Sweden, and Denmark**. This overrides the general rule that no marital deduction is allowed to a U.S. non-domiciliary.

Domiciliaries from **Austria, Germany, and Sweden** are provided with **special relief regarding indebtedness**. Debt related to the acquisition and upkeep of U.S. property, whether secured or unsecured, are fully deductible from the value of the property.

If a married couple immigrated from a community property jurisdiction, then it is crucial that these rules be carefully examined as an equal interest in the marital property may be included in the estate of the decedent spouse. Joint ownership may support non application of community property rules. Although not a treaty provision, joint ownership in property can also support exclusion of U.S. property if the estate can prove that the surviving co-owners were the individuals who contributed towards the purchase of the U.S. property.

b. Gift Taxes for Non-Domiciliary Aliens – A Planning Opportunity

Non-domiciliary aliens are subject to U.S. gift tax on the transfer of U.S. real or tangible personal property. However, **gifts of U.S. intangible assets by non-domiciliary aliens are not subject to U.S. gift tax. This exception includes gifts of foreign corporation shares as well as gifts of U.S. corporation shares even though the shares of a U.S. corporation would be taxable in the estate of a non-domiciliary decedent.**

There is an annual exclusion of $14,000 per recipient (or higher for spouses – see Table F-1) on taxable gifts of "U.S. property." This annual exclusion, which is adjusted annually for cost of living, is available to all donors for gifts to all donees, including non-domiciliaries and non-citizens with one important exception. Non-domiciliaries are not entitled to the "gift splitting" benefit to which U.S. citizens and resident aliens are entitled.

Non-domiciliaries are also not entitled to the unlimited marital exclusion available to U.S. citizens. Instead, there is a $143,000 exclusion amount for gifts made in 2013 to non-U.S. citizen spouses (See Table F-1).

Gifts made by non-domiciliaries of non-U.S. property to U.S. residents are not subject to the U.S. gift tax but may be subject to disclosure requirements. The filing of information return Form 3520 will be necessary if the amount of the gift exceeds $100,000 in any year (see Question F, 3) for 2010. Gifts that are generally free of tax would be taxable and severely penalized if Form 3520, discussed later, is not filed when required.

5. STATE TREATMENT OF ESTATE AND GIFT TAXES

Until federal legislation changed, which we describe more fully below, all states imposed estate, gift, and/or inheritance taxes. All states that imposed estate taxes did so up to the amount of the federal credit allowed under prior federal law. Some states also imposed additional inheritance or estate taxes. In 2001 federal legislation passed which repealed the state death tax credit. Accordingly, there is no longer a state level estate tax imposed by states whose systems were solely "coupled" to federal law (e.g., states that based their estate tax systems solely on the federal credit since repealed). Some of these "coupled" states have implemented legislation to "decouple" from the federal system by basing their respective state level estate taxes on federal law as it existed prior to the tax law change or opting to implement only portions of the 2001 federal legislation to allow for the state to maintain a state level tax.

Currently, Florida, along with Alabama and Nevada, are the only "coupled" states that require a state constitutional amendment to take action to decouple. To date, such an amendment has not been passed, and these states remain unable to impose a state level estate tax for persons dying after December 31, 2004 because the tax systems are directly correlated with the federal state tax credit which has been repealed.

Some states impose an inheritance tax which actually taxes the beneficiaries on what they receive, rather than the estate itself. The primary responsibility for filing the inheritance tax return and paying the tax usually falls on the personal representative of the estate.

As of 2015, the following states no longer impose a state level estate tax. Furthermore, these states do not impose an inheritance tax:

Alabama	Florida	Montana	Texas
Alaska	Georgia	Nevada	Utah
Arizona	Hawaii	New Hampshire	West Virginia
Arkansas	Idaho	New Mexico	Wyoming
California	Michigan	North Dakota	
Colorado	Mississippi	South Carolina	
Delaware	Missouri	South Dakota	

Connecticut, Louisiana, North Carolina, and Tennessee are the only states that currently impose state level gift taxes.

These taxes are a significant consideration in accurately calculating tax due on any estate and are not considered in the sample calculations herein because the laws vary greatly by state.

Note: Please see Question Q for a list of countries that have estate and gift tax treaties with the U.S. These treaties may eliminate or reduce exposure to U.S. estate tax.

F Continued

Table F-1

Gift Tax Exclusions and Deductions
Applicable For Gifts to Spouse Given By:

U.S. Property Given To:	U.S. Citizen Spouse	Domiciliary Alien Spouse	Non-Domiciliary Alien Spouse
U.S. Citizen Spouse	Unlimited Marital Deduction	Unlimited Marital Deduction	Unlimited Marital Deduction
Domiciliary Alien Spouse	$143,000 Annual Exclusion	$143,000 Annual Exclusion	$143,000 Annual Exclusion
Non-Domiciliary Alien Spouse	$143,000 Annual Exclusion	$143,000 Annual Exclusion	$143,000 Annual Exclusion
Non-U.S. Property Given To:			
U.S. Citizen Spouse	Unlimited Marital Deduction	Unlimited Marital Deduction	Not Taxable
Domiciliary Alien Spouse	$143,000 Annual Exclusion	$143,000 Annual Exclusion	Not Taxable
Non-Domiciliary Alien Spouse	$143,000 Annual Exclusion	$143,000 Annual Exclusion	Not Taxable

F Continued

Table F-2

Unified Rate Schedule for 2015

COLUMN A TAXABLE AMOUNT OVER	COLUMN B TAXABLE AMOUNT NOT OVER	COLUMN C TAX ON AMOUNT IN COLUMN A	COLUMN D RATE OF TAX ON EXCESS OVER AMOUNT IN COLUMN A (PERCENTAGE)
$ 0	$ 10,000	$ 0	18%
10,000	20,000	1,800	20%
20,000	40,000	3,800	22%
40,000	60,000	8,200	24%
60,000	80,000	13,000	26%
80,000	100,000	18,200	28%
100,000	150,000	23,800	30%
150,000	250,000	38,800	32%
250,000	500,000	70,800	34%
500,000	750,000	155,800	37%
750,000	1,000,000	248,300	39%
1,000,000	---	345,800	40%

F Continued

Table F-3

The following examples will illustrate the transfer tax differential for taxable transfers by domiciliary or non-domiciliary aliens in 2013:

	EXAMPLE 1	EXAMPLE 1	EXAMPLE 2	EXAMPLE 2
	U.S. CITIZEN OR DOMICILIARY ALIEN	NON-DOMICILIARY ALIEN	U.S. CITIZEN OR DOMICILIARY ALIEN	NON-DOMICILIARY ALIEN
Taxable Estate or Gift	$ 5,250,000	$ 5,250,000	$ 7,500,000	$ 7,500,000
Exemption Equivalent of Unified Credit Available	(5,250,000)	(60,000)	(5,250,000)	(60,000)
Estate Tax Due	-------------	2,045,800	845,800	2,921,800

6. GIFTS FROM FOREIGN SOURCES TO U.S. CITIZENS AND U.S. RESIDENT ALIENS

U.S. law mandates that U.S. persons report the **receipt of gifts from foreign** "persons" (e.g., entities) other than individuals or estates (such as **trusts and corporations**) on Form 3520 if the **aggregate** of these receipts exceeds **$15,358** in 2014. Qualifying medical and educational receipts paid directly to the respective institutions are excluded from this reporting requirement. Gifts or bequests received from foreign **individuals** and **estates** are not required to be reported unless such receipts exceed **$100,000** for the year.

The consequences of failure to file information returns to report gifts from foreign persons are similar to the consequences of failure to file information returns to report distributions from foreign trusts (as described in Question K). In both situations, **Internal Revenue Service is given the authority to treat a non-taxable receipt as a taxable receipt** and in the case of gifts, to impose a penalty of 5% of the value of the gift for each month or portion thereof after the due date for the information return, up to a **maximum penalty of 25%**. **Thus the cost of not reporting a gift from a foreign source could be 65% of the gift (40% tax plus 25% penalty)**.

G. WHAT ARE THE RATES OF U.S. INCOME AND OTHER TAXES IMPOSED UPON INDIVIDUALS AND THE VARIOUS FORMS OF ENTITIES INVESTING IN THE U.S.?

1. U.S. SOURCE INCOME VERSUS EFFECTIVELY CONNECTED INCOME

a. Withholding Taxes on Non-U.S. Payees of U.S. Source Income

Federal withholding taxes imposed on **U.S. source income** paid to a non-resident alien are **30% (or lower treaty rate) on dividend and interest income, and on rental and royalty income.**

The Internal Revenue Service requires withholding at a rate of 30% **on all proceeds distributed to non-residents** who have not properly completed a Form W-8BEN when required. These proceeds can include dividends **as well as proceeds that are generally exempt from withholding** such as bank interest, and **the entire proceeds from sales of securities regardless of gains or losses**. Payments of proceeds will not be subject to withholding if Form W-8ECI (Certificate of Foreign Person's Claim for Exemption From Withholding on Income Effectively Connected With the Conduct of a Trade or Business in the United States) is filed with the withholding agent (See Question G, 1, b).

Form W-8BEN allows payors of U.S. source income to rely on the foreign status assertion an individual represents by completing the form. It also allows for the payors to withhold at reduced withholding rates, if applicable, when the non-resident claims they are residents of a treaty country with the U.S.

If payors received a properly completed Form W-8BEN, **federal withholding rates** imposed on **U.S. source income** paid to a non-resident alien are 30% (or lower treaty rate) on **dividends, rental and royalty income**. Bank and "portfolio interest" would be exempt from withholding as would sales proceeds of securities. **Other interest** would be subject to the 30% rate.

Form W-8BEN requires only the name and foreign address (place of tax residence) of the account holder. An individual taxpayer identification number (ITIN) is required if the non-resident is requesting that tax treaty benefits apply to reduce withholding (See Appendix B). An ITIN is also required for other exemptions relating to annuities under IRC 871(F).

Recent experience indicates that U.S. banks and financial institutions applying the "know-your-client approach" are challenging the validity of W-8BENs filed by non-U.S. persons and in some cases, remitting 30% of portfolio assets to IRS without the consent of the client. Moreover, numerous U.S. banks and financial institutions are refusing to open accounts for non-U.S. persons and corporations. Their counterparts in foreign jurisdictions likewise are refusing to deal with U.S. persons and corporations. This situation has intensified since the UBS scandal (See Question N, 4) but had its roots in the Treasury Regulation issued in 2000 which introduced the concept of "qualified intermediary" status for banks and other financial institutions. The goal of the U.S. Treasury is complete transparency in worldwide banking. The adverse effect of this ambitious goal on world commerce is clearly being felt.

Form W-9, which U.S. citizens or residents complete to verify their U.S. tax residency in order to have all proceeds subject to a 30% withholding rate, requires a name, address, and social security number, or ITIN.

Rental income received by a foreign entity or individual property owner is generally subject to withholding. The exception to this rule is if the rental income is considered to be effectively connected income (described below).

There is a similar **withholding on partnership and LLC profits** which are deemed to be allocated to foreign partners. The U.S. partnership and LLC are required to remit taxes quarterly for each foreign partner at the highest income tax rate applicable to the foreign partner. For 2013, the **rate for foreign individual partners as well as foreign corporate partners is 39.6%.** These remittances of tax withheld are required quarterly **without regard to distributions**. However, as a result of claims for many years that partners are subject to over-withholding, foreign partners may now certify net operating loss carryovers attributable to prior years in order to reduce the withholding burden in the current year.

An exception to quarterly withholding is if the partnership is a withholding foreign partnership that files Form 1042S or if the foreign partnership has issued a certificate which makes it justifiable for a withholding agent to deem the payments as resulting from the conduct of U.S. trade or business. Another exception to quarterly withholding is if the foreign partner submits Form 8804-C to the partnership certifying that the partner has other deductions or losses that reduce or eliminate the withholding. Form 8804-C must be provided by the foreign partner on an annual basis.

Resident aliens and non-resident aliens and foreign corporations with "**effectively connected**" U.S. income are taxed at the rates described in Question G, 2, and 3.

b. Effectively Connected Income

Withholding is not required on income "**effectively connected**" with a U.S. trade or business. **Such income is taxable and is reported on a U.S. tax return at graduated tax rates rather than the general 30% withholding rate**. Form W-8ECI must be filed with the withholding agent or payer to ensure that effectively connected proceeds are not subject to withholding and are taxed at graduated rates when the appropriate U.S. income tax return is required to be filed.

Rental income received by a foreign corporation or individual property owner can claim this income as "effectively connected" income exempt from withholding by timely filing Form W-8ECI which states that the recipient is conducting a U.S. trade or business and is, therefore, exempt with withholding. **An ITIN is required to complete this form. Refer to Appendix B for further information. The conduct of a U.S. trade or business requires a U.S. income tax return be filed annually for the business**.

Additionally, the activity must be considered under U.S. tax laws to reach a level where a trade or business is considered to be conducted. Because there is no precise definition of what level of activity is sufficient for a U.S. trade or business to exist, the Internal Revenue Service allows for a special election to be made by individuals and corporations.

A foreign individual or foreign corporation can elect to have a U.S. rental activity deemed to constitute a U.S. trade or business if an election is made with a timely U.S. income tax return filing. No special treaty provision to qualify is necessary for this election. **This election can only be made for a taxable year if the taxpayer has income from U.S. real property** and will thereafter continue in effect unless properly revoked, even though during a subsequent year there is no applicable real property income.

Another election is available for **corporations** under IRC Section 897(i), which allows a qualifying foreign corporation to be treated as a domestic corporation and deems the electing corporation to be in a U.S. trade or business and thereby not subject to withholding under the Foreign Investment in Real Property Tax Act (FIRPTA) on the disposition of U.S. real property. This election must contain the U.S. employer identification number (EIN), name, and address of the foreign corporation. If the foreign entity does not have an EIN, then one must be obtained in order for the election to be valid. Additionally, **this election is possible only if a qualifying non-discrimination provision exists in a treaty**.

Generally, a foreign corporation in a qualifying treaty country must be beneficially owned by residents of that country to qualify for the treaty benefits. The “limitation of benefits” section of the applicable treaty should be consulted. Use of treaties by non-residents of the treaty country is called “treaty shopping” and, in many cases, voids the application of treaty benefits.

Netherlands Antilles corporations (since September 1, 1988) and Barbados (since January 1, 2994) no longer qualify for the “treaty shopping” corporation IRC 897(i) election.

For a sale of a U.S. real property interest, the withholding tax rate is **10% of the gross sales price irrespective of what the actual tax liability from the sale may actually be**. This 10% withholding tax is one of the provisions of the Foreign Investment in Real Property Tax Act (FIRPTA) legislation enacted as an enforcement mechanism to collect tax on any realized gain from the disposition of U.S. real property by non-resident individuals. Gains may qualify for long-term capital gains rates which are currently at 20% of the property is held by individuals while corporations are taxed at a maximum federal rate of **39.6%**. **Reference Appendix A for instances where the withholding remitted directly to the Internal Revenue Service can be reduced to the actual lower tax liability and filing requirements that would be involved.**

Most states tax corporate and individual gains on sale of real property. Some states also impose withholding taxes on a sale of real estate.

G Continued

2. INDIVIDUAL TAX RATES ON ORDINARY TAXABLE INCOME AND INCOME EARNED FOR SERVICES

a. The 2015 federal income tax rates on ordinary taxable income for individuals are as follows:

Joint with Spouse	**Tax Rate**
$0 to $17,850	10% of taxable income
$17,851 to $72,500	$1,785.00 + 15% of excess over $17,850
$72,501 to $146,400	$9,982.50 + 25% of excess over $72,500
$146,401 to $223,050	$28,457.50 + 28% of excess over $146,400
$223,501 to $398,350	$49,919.50 + 33% of excess over $223,050
$398,351 to $450,000	$107,768.50 + 35% of excess over $398,350
Over $450,000	$125,846 + 39.6% of excess over $450,000

Single Persons	**Tax Rate**
$0 to $8,925	10% of taxable income
$8,926 to $36,250	$892.50 + 15% of excess over $8,925
$36,251 to $87,850	$4,991.25 + 25% of excess over $36,250
$87,851 to $183,250	$17,891.25+ 28% of excess over $87,850
$183,251 to $398,350	$44,603.25 + 33% of excess over $183,250
$398,351 to $400,000	$115,586.25 + 35% of excess over $398,350
Over $400,000	$116,163.75 + 39.6% of excess over $400,000

Head of Household	**Tax Rate**
$0 to $12,750	10% of taxable income
$12,751 to $48,600	$1,275.00 + 15% of excess over $12,750
$48,601 to $125,450	$6,652.50 + 25% of excess over $48,600
$125,451 to $203,150	$25,865.00 + 28% of excess over $125,450
$203,151 to $398,350	$47,621.00 + 33% of excess over $203,150
$398,351 to $425,000	$112,037.00+ 35% of excess over $398,350
Over $425,000	$121,364.50 + 39.6% of excess over $425,000

Married Filing Separately	**Tax Rate**
$0 to $8,925	10% of taxable income
$8,926 to $36,250	$892.50 + 15% of the excess over $8,925
$36,251 to $73,200	$4,991.25 + 25% of the excess over $36,250
$73,201 to $111,525	$14,228.75 + 28% of the excess over $73,200
$111,526 to $199,175	$24,959.25 + 33% of the excess over $111,525
$199,176 to $225,000	$53,884.25 + 35% of the excess over $199,175
Over $225,000	$62,923.00 + 39.6% of the excess over $225,000

G Continued

b. Income earned for services performed is subject to additional payroll or self-employment taxes as follows:

2013: Earnings base up to $113,700 – FICA (social security tax)
2013: Earnings base for Medicare tax is unlimited

The 2013 payroll tax rates are as follows:

Self employed: 12.4% FICA and 2.9% Medicare tax (half is tax deductible)

Employees: 6.2% of earnings base employer's share of FICA tax
6.2% of earnings base employee's share of FICA tax
1.45% of earnings employer's share of Medicare tax
1.45% of earnings employee's share of Medicare tax

Effective January 1, 2013, the following two surtaxes take effect.

(1) 0.9% hospital insurance tax will be charged against wages and self-employment earned in excess of $250,000 per married couple ($125,000 single individual)
(2) 3.8% Medicare contribution tax imposed on unearned income of individuals, estates and trusts over a threshold amount ($250,000 married/$125,000 single); the tax will be assessed on the lesser of net investment income or the excess of modified adjusted gross income over the threshold amount

Standard Federal Income Tax Deduction (if deductions are not itemized) - 2012 and 2013

2012	2013
Single - $5,950	Single - $6,100
Married filing jointly - $11,900	Married filing jointly - $12,200
Married filing separately - $5,950	Married filing separately - $6,100
Head of household - $8,700	Head of household - $8,950

Exemptions: $3,800 per dependent (2012)
$3,900 per dependent (2013)

The personal exemption is subject to phase-out for high income taxpayers ($250,000+).

3. CORPORATE TAX RATES ON TAXABLE INCOME

The federal tax rates for taxable income of "C" corporations are as follows:

	Tax Is	Of the Amount Over
$0 - $50,000	15%	$0
$50,000 - $75,000	$7,500 + 25%	$50,000
$75,000 - $100,000	$13,750 + 34%	$75,000
$100,000 - $335,000	$22,250 + 39%	$100,000
$335,000 - $10,000,000	$113,900 + 34%	$335,000
$10,000,000 - $15,000,000	$3,400,000 + 35%	$10,000,000
$15,000,000 - $18,333,333	$5,150,000 + 38%	$15,000,000
$18,333,333 and over	35%	$0

Note: Personal service corporations are taxed at a flat rate of 35% of taxable income (See Question G, 4).

Florida corporations, other than S corporations, LLC and IC-DISC corporations, are taxed on their taxable income in excess of $25,000 by the State of Florida at a rate of 5.5%.

These corporate tax rates also apply to foreign corporations doing business in the U.S. Such foreign corporations are also subject to the Federal Branch Profits Tax unless treaty protection applies. (See Question G, 16 and Question O, 1, b for further information.)

Most foreign corporations form U.S. subsidiaries in the U.S. to avoid the branch profits tax. However, this does not avoid the withholding tax on dividends, other than liquidating distributions.

4. PERSONAL SERVICE CORPORATIONS

A personal service corporation is a "C" corporation whose principal activity is the performance of personal services, such as health services, law, engineering, architecture, accounting, actuarial services, performing arts, or consulting services. Also, these services must be substantially performed by employee-owners and more than 10% of the fair market value of its outstanding stock must be owned by employee-owners on the last day of the testing period for the tax year.

A personal service corporation is required to file income tax returns on the calendar year and to pay income tax at 35% with no benefit of the lower progressive rates available to other "C" corporations. Most personal service businesses choose to operate as "S" corporations (See Question G, 7) or LLCs or partnerships (including LLPs) (See Question G, 8) to avoid this problem.

5. PERSONAL HOLDING COMPANY

A personal holding company is a "C" corporation, which is closely held and whose income is largely of investment character. Earnings of a personal holding company that are not distributed are subject to a **penalty tax** of 20% in addition to the regular corporate income tax. Classification as a personal holding company is a two-part test:

a. **Stock Ownership Test** – more than 50% in value of the corporation's outstanding stock was owned directly or indirectly, by five or fewer individuals at any time during the last half of the taxable year.

b. **Income Test** – 60% or more of the corporation's "adjusted ordinary gross income" is "personal holding company income." These terms are specifically defined in the Internal Revenue Code, but for the most part, "personal holding company income" is income that is largely of an investment nature, such as interest, dividends, rents, royalties and other receipts of a passive nature. There are several additional rules and definitions pertaining to personal holding companies, but in general, corporations should **annually** review their vulnerability to this punitive tax. **The penalty tax is avoided by having the corporation declare a dividend to its shareholders which is taxable to those shareholders.**

6. EXPORT CORPORATIONS

a. "IC-DISC" – Interest Charge Domestic International Sales Corporation

An IC-DISC (Interest Charge Domestic International Sales Corporation) **defers its profits from federal income taxes at the corporate level** on the first $10,000,000 annually of qualified export receipts. IC-DISC **tax deferred profits** are not taxed to its shareholders until distributed or invested in non-qualified property. This enables the IC-DISC to accumulate capital from profits on a "tax deferred" basis. **In essence, the IC-DISC can use deferred income taxes to fund the capital necessary to expand the export business.** This gives the IC-DISC an advantage over a non-IC-DISC foreign export corporation doing business in the U.S. which is taxed on export income from its U.S. operations under the "effectively connected" rule.

The amount of tax deferred is calculated at the tax rate of the shareholder and treated as if that tax was borrowed by the shareholder from the U.S. Treasury subject to an interest charge. The interest charge on this amount of tax deemed to be borrowed must be paid annually by the shareholder. The interest rate charged is based on the base period T-bill rate on 1-year T-bills auctioned during the period ended September 30th of the current year compounded daily for the number of days in the shareholder's taxable year. For 2012, the base period rate was 0.16%.

There are no restrictions on who can be an IC-DISC shareholder, including foreign persons or tax exempt entities. However, certain types of corporations are not eligible to be treated as an IC-DISC, including "S" corporations, personal holding companies, tax exempt corporations and, in general, banks, insurance companies, and mutual and investment cooperatives. **The IC-DISC election must be made within 90 days after formation of the IC-DISC corporation or not later than 90 days after the beginning of the year the IC-DISC election is to become effective.**

A corporation can qualify as an IC-DISC if at least 95% of its gross receipts are qualified export receipts, sales of property or certain services (engineering or construction services for foreign facilities and, in certain cases, managerial services in furtherance of the production of other qualified export receipts of an unrelated DISC) outside of the U.S. or its territorial possessions. Export property is property (a) manufactured, produced, grown, or extracted in the U.S.; that is (b) held primarily for sale, lease, or rental, in the ordinary course of a trade or business for direct use, consumption or disposition outside the U.S.; and (c) whose fair market value does not constitute more than 50% of imported articles.

Also, 95% of the corporation's assets at the end of the taxable year must be qualified export assets (used in the generation of qualified export receipts; i.e., inventory, trade, accounts receivable, et al). An IC-DISC can qualify under this test regardless of the amount of non-export assets held during the tax year as long as the excess assets are not held at the close of the tax y ear. But any gain on the disposition of this excess does not constitute qualified export receipts for purposes of the 95% qualified export receipts test.

An IC-DISC may make a current distribution to shareholders to reduce the adjusted basis of unqualified assets enough to meet the 95% test. Also, an IC-DISC which fails to meet the qualified export assets test may retroactively qualify as an IC-DISC by making a late paid dividend distribution equivalent to the fair market value of all unqualified assets.

Distributions of IC-DISC profits to shareholders are taxed to the shareholder at the shareholder's rate in the year of distribution – a single level of taxation. The earnings and profits are currently taxed at a 20% rate. This makes an IC-DISC a singularly attractive tax device for those who trade in qualified exporting of U.S. products and services.

b. Foreign Sales Corporation (FSC)

The American Jobs Creation Act of 2004 repealed the Extraterritorial Income Exclusion system of tax benefits that were originally enacted in 2000 to replace the Foreign Sales Corporation (FSC) regime. In late 1997, the European Union (EU) challenged the FSC as an illegal export subsidy under the World Trade Organization's (WTO) rules. Following a 2000 WTO ruling in favor of the E.U., the U.S. passed the FSC Repeal and Extraterritorial Income Exclusion Act of 2000 (ETI Act) to replace the FSC regime. The EU immediately challenged the ETI Act. The ETI Act was ruled illegal by the WTO in 2002.

7. "S" CORPORATIONS

An "S" corporation is a **pass-through entity** that usually pays no state income tax in most states, including Florida, and no federal income tax at the entity level. The shareholder pays the income tax on "S" corporation income at the individual tax rates previously described (maximum 39.6%). **"S" corporations *must be owned by U.S. citizens, resident aliens or certain types of qualifying domestic trust.*** In the future, proposed regulations may allow for individuals who rely on an income tax treaty to be considered a U.S. non-resident to, nevertheless, qualify as an S corporation shareholder (See Question D). The "tie-breaker" individual would have to enter into a withholding agreement with the S corporation to withhold income tax on the shareholder's pro-rata share of income from the company and make appropriate deposits to the Internal Revenue Service.

A maximum of 100 shareholders are permitted to own an "S" corporation. For purposes of the membership requirement, certain family members are treated as one shareholder.

"S" corporation status must be elected by the 15th day of the third month of the tax year, if the election is filed during the tax year the election is to take effect, or the election may be filed at any time during the preceding tax year. An election made after the 15th day of the 3rd month but before the end of the tax year is effective for the next year. **Late elections may now be accepted under certain circumstances**.

In some circumstances, "S" corporations are subject to federal income tax at the corporate level. This can occur if they were formerly "C" corporations and then elect "S" status. **Care must be taken when forming a corporation to properly file the "S" election.**

Some states tax "S" corporations on their income. Some states tax "S" corporation shareholders on the income of the "S" corporation whether or not the shareholders are residents of those states (See Table P-2).

8. LIMITED LIABILITY COMPANIES (LLCs) AND LIMITED PARTNERSHIPS (LPs)

Foreign investors in the U.S. who are barred from "S" corporation ownership (See Question G, 7) **often find an alternative structure in the Limited Liability Company (LLC)** or in the **Limited Partnership (LP)**. These are "pass-through" entities that eliminate the second level of tax imposed upon "C" corporation dividends (See Question G, 11). Regrettably, the imposition of withholding taxes upon partnership profit allocable to non-residents (See Question G, 1) can make this a less attractive structure than appears at first glance.

LLCs differ from LPs in that no general partner who has unlimited liability need be designated. In common practice, the "general partner" of an LP has usually been a corporation with minimal capital. Most states recognize LLCs as partnerships for federal tax purposes and, as such, they pay no state income tax at the entity level. The individual partners of LLCs and LPs report and pay federal and state income tax on the income generated by these entities at individual tax rates (corporate partners pay at corporate rates). LLCs and LPs which possess no more than two of the following corporate characteristics are treated as **pass-through** entities for federal income tax purposes and by most of the states:

1. Limited liability
2. Centralized management
3. Continuity of life
4. Free transferability of interests

G Continued

Most LLCs and LPs [including Limited Liability Partnerships (LLPs)] avoid characteristics #3 and #4 above in their formation documents, thus avoiding being treated as corporations for federal income tax purposes. General partnerships lack characteristic #1 above and usually lack two or three of the remaining characteristics.

As of April 30, 1997, all states have enacted LLC legislation. Notwithstanding federal income tax treatment of the LLC as a partnership, some states tax the LLC as a corporation. Some states **tax partners on their partnership income** whether or not the partners are residents of those states.

The “Check-the-Box” regulations permit a federal tax election for unincorporated entities with more than one owner to choose to be taxed as a partnership or as a corporation. Foreign entities may make the same election provided their business formation is not one listed by U.S. taxing authorities as being a “per se” corporation (Treasury Regulation 301.7701-3). Single member LLCs unless electing to be treated as a corporation, are disregarded for U.S. income tax purposes, even though they remain valid for other purposes. Thus, a foreign corporation owning a single member LLC not electing to treat it as a corporate subsidiary is regarded as having a U.S. branch operation for income tax purposes. An individual in that situation, for tax purposes, is regarded as conducting the activities of the LLC personally.

9. TRUSTS

The person who creates a trust is referred to as the grantor or settler. If the grantor retains powers and benefits for himself, the trust is called a **grantor trust and trust earnings are reported as being earned by the grantor directly rather than the trust**. Trusts may be designated as revocable or irrevocable. All trusts are deemed to be grantor trusts as long as the grantor retains the power to revoke the trust and retain the assets as his or her own.

Trusts are taxed at the trust level if they are non-grantor trusts.

Trust tax rates for capital gains on long-term investments are a maximum of 20%. Non-grantor trusts are taxable on all other undistributed worldwide income at the rates described below for the tax year 2013.

$0 to 2,450	15% of taxable income
$2,451 to $5,700	$367.50 + 25% of excess over $2,450
$5,701 to $8,750	$1,180.00 + 28% of excess over $5,700
$8,751 to $11,950	$2,034.00+ 33% of excess over $8,750
Over $11,950	$3,090.00 + 39.6% of excess over $11,950

G Continued

Trusts may be categorized as either a domestic or foreign trust. A trust is considered a **domestic trust** if two tests are satisfied: (1) U.S. Court Test, and (2) U.S. Control Test. Generally, both tests are met if a court within the U.S. is able to exercise primary supervision over the administration of the trust, and one or more U.S. persons have the authority to control ass substantial decisions of the trust. A trust not meeting both tests is considered a **foreign trust**.

U.S. individuals who transfer appreciated property to foreign non-grantor trusts will, for federal income tax purposes, be required to treat such a transfer as a sale for an amount equal to the fair market value of the property transferred. This is the case even if no consideration is received in exchange for the transferred property. The U.S. transferor is required to recognize as gain the excess of the fair market value of the property transferred, over the transferor's adjusted basis (See Question G, 15). This rule does not apply to transfers by U.S. persons of property to foreign grantor trusts. The use of foreign grantor trusts is discussed in Question K.

A legacy trust is a vehicle for a settlor of the trust to set aside all incidences of ownership of certain assets for the benefit of other individuals, generally relatives. For a U.S. citizen or domiciliary alien, a transfer to such a trust is a taxable gift (subject to limited exemptions). For a non-resident alien such a transfer (except for transfers of U.S. real property interests already held) is a gift that is not subject to U.S. gift taxes. Properly constructed it assures that the property will not be subject to U.S. estate taxes.

This type of transfer is common for single parcels of property the purchase of which is funded by the settler through a trust for the benefit of one or more children. Often a foreign trustee is selected which makes the trust a foreign trust. The advantage of the arrangement is that any income earned by the trust is taxed once at individual tax rates (similar to corporate rates, but without the withholding tax on distributions) and the capital gain rate on sale of the property is taxed at the individual rate which now is less than half the corporate rate. The limitation with this arrangement is that the trust often ends with a distribution of assets, which is then included in the estate of the recipient when they die. Since the estate tax exemption for non resident aliens is only $60,000 in most cases, this is a burden.

The legacy trust holds the assets beyond the death of certain future beneficiaries. Now that more and more states have laws repealing laws against perpetuities (Florida allows trusts with lives of 360 years) we think more and more family trusts will be established which will avoid mandatory distributions that will mean avoiding of estate taxes on many future generations of heirs.

We would be pleased to share more information on this structure upon individual request.

10. CAPITAL GAINS TAX RATES

Short-term capital gains rates apply to capital property sold with a holding period of less than 12 months. The applicable tax rates for these gains are equal to the ordinary income rates listed in Question G, 2, a (individuals) and Question G, 9 (trusts).

Individual and trust tax rates for capital gains on dispositions of long-term investments and on certain dispositions or licensing of patents and other intellectual property are a maximum rate of 20%, plus applicable state income taxes (of which there are none in Florida for individual taxpayers). The holding period required to qualify for long-term capital gain treatment is 12 months. A 0% long-term capital gains rate is available to lower income individuals.

A 25% rate is applied to depreciation previously claimed and calculated on a straight-line basis when investment property is sold. Depreciation claimed on investment property is taxed at ordinary income rates to the extent that the allowance was calculated using an accelerated method of depreciation which exceeds the straight-line basis. This provision becomes relevant, for instance, when rental property for either residential or commercial purposes which was depreciated (under the ACRS depreciation system) is sold.

A 28% rate is applied to gains on the sale collectibles, including certain coins.

There is no preferential capital gain tax rate for **corporations**. The maximum regular tax rate for corporations is 35%, plus applicable state income taxes.

Note that sales of depreciable property to related parties, such as rental real estate, are taxed at ordinary tax rates and not at the lower capital gains rate.

11. DOUBLE TAXATION BY THE U.S. – "C" CORPORATIONS

A "C" corporation is an entity subject to double taxation. The first level of tax occurs when the corporation, as its own separate entity, pays tax on net income based on the rates described in Question G, 3 above. A second level of tax occurs when dividends are paid by the corporation to its shareholders. Prior to legislation enacted in 2003, **dividends** were taxed at ordinary federal tax rates as high as 38.6%. Including state taxes, the **combined** tax rate on ordinary income had previously been combined for an approximate aggregate tax rate of 50 – 70%. The 2003 tax legislation lessened this burden substantially.

The 2003 legislation has changed the way dividends are taxed. Rather than being subject to the higher ordinary tax rates, qualifying dividends (See Question G, 12) are not subject to a flat 20% rate (or as low as 0% for low income shareholders). Effectively, between the entity level tax, dividends, and the State of Florida corporate tax, the maximum combined tax rate now in effect is approximately 50% - 55% (higher in many other states).

Since 1986, this same concept of double taxation also applies to sales and/or liquidations of "C" corporations. The "C" corporation is taxed on the **gain on sale or liquidation** at maximum corporate rates and generally any **individual U.S. shareholder** is taxed again on the liquidating distribution at 20% plus state taxes for a combined tax rate which can exceed 50%. **Non-resident alien shareholders** are usually not taxed on gains on sale of shares or on liquidating distributions under current tax law and will face a total tax not exceeding 40% at the corporate level (in Florida) (See Question E, 1, a and E, 2 d).

It is worthy to note that (a) income distributions and (b) distributions from sales or liquidations of "S" corporations, IC-DISC corporations, LLCs, and partnership interests held by individuals generally result in **no double taxation** and, in states such as Florida, result in a maximum tax rate of (a) 39.6% (effectively greater than 40% for higher income taxpayers) on income distributions and (b) 20% for capital gain liquidating distributions, respectively.

Nearly all publicly traded U.S. corporations and foreign owned U.S. corporations are "C" corporations.

12. DIVIDENDS

The taxation of dividends changed substantially with the passage of the Jobs and Growth Tax Relief Reconciliation Act of 2003. Instead of being taxed at ordinary tax rates which had previously been as high as 38.6% prior to tax year 2003, qualifying dividends are now taxed utilizing the same tax rate as capital gains, which are 20% and 0% for lower income individuals for qualifying dividends received during 2013.

Qualifying dividends are dividends received during the tax year from domestic corporations and qualified foreign corporations, meet a specific holding period, and are not otherwise disqualified dividends as described below.

Qualified foreign corporations include:

- Corporations incorporated in a U.S. possession, or

- Corporate shares that are readily tradable on an established U.S. securities market or that are eligible for benefits of a comprehensive income tax treaty with the U.S. where there is an exchange of information provision and which the Internal Revenue Service determines is satisfactory for purposes of the qualified dividend rules. These countries include:

Australia	Estonia	Italy	New Zealand	Spain
Austria	Finland	Jamaica	Norway	Sri Lanka
Bangladesh	France	Japan	Pakistan	Sweden
Barbados	Germany	Kazakhstan	Philippines	Switzerland
Belgium	Greece	Korea	Poland	Thailand
Canada	Hungary	Latvia	Portugal	Trinidad & Tobago
China	Iceland	Lithuania	Romania	Tunisia
Cyprus	India	Luxembourg	Russian Federation	Turkey
Czech Republic	Indonesia	Mexico	Slovak Republic	Ukraine
Denmark	Ireland	Morocco	Slovenia	United Kingdom
Egypt	Israel	Netherlands	South Africa	Venezuela

Qualified foreign corporations do not include passive foreign investment companies (See Question M, 7).

The holding period for qualifying dividends is met if a shareholder owns stock long enough. **For common stock**, a taxpayer must own the stock for more than 60 days during the 121-day period beginning 60 days before the ex-dividend date. **Preferred stock** must be held more than 90 days during the 181 day period that begins 90 days before the ex-dividend date if the dividends are attributable to periods totaling more than 366 days. If the preferred dividends are attributable to periods totaling less than 367 days, the 60-day holding period discussed previously applies.

Additionally, the following are not considered "qualifying dividends:"

- Capital gain distributions.
- Dividends paid on deposits with mutual savings banks, cooperative banks, credit unions, U.S. building and loan association, U.S. savings and loan associations, federal savings and loan associations, and similar financial institutions. These amounts are reportable as interest income.
- Dividends on any share of stock to the extent that the taxpayer is under an obligation to make related payments with respect to positions in substantially similar or related property.
- Any amount taken into account allowing the dividend to support a deduction for investment interest.
- Dividends from certain tax exempt corporations.
- Dividends paid by an Employee Stock Ownership Plan (ESOP).
- Payments in lieu of dividends if the shareholder knows or has reason to know that the payments are not qualified dividends.

Qualifying dividends cannot be reduced by any capital losses, but $3,000 of capital losses are generally allowable to reduce ordinary income if no capital gains exist to be offset.

If the 20% rate is claimed for dividends, they are not included in net investment income for purposes of determining the deductibility of investment interest. An election to forego the 20% rate can be made if the investment interest expense deduction would be more advantageous.

13. SALES TAXES, EXCISE AND VALUE-ADDED TAXES (VAT)

There is no VAT tax in the U.S. However, state and local governments impose sales taxes on most purchases of goods and some services. Rates vary from zero to 11%. Excise taxes are generally imposed on the purchase price of certain goods (such as fuel), similar to VAT taxes.

To provide some relief to residents of states that do not have a personal income tax (Florida, Nevada, South Dakota, Alaska, Washington, and Wyoming), the American Jobs Creation Act of 2004 implemented provisions to allow for individuals to deduct state and local sales taxes if they itemize and elect not to deduct state or local income taxes. Prior to this legislation, deductions were only allowed for state or local income taxes generally providing deductions to residents of states that had individual state and local income tax systems. Taxpayers who pay less in state income taxes than sales tax may benefit by deducting the sales tax although there will be a greater recordkeeping requirement.

The IRS has issued tables to calculate and claim the sales tax deduction. If actual expenses prove greater than the tables, the taxpayer can utilize this higher figure. Receipts will be required to be maintained by the taxpayer if the table is not utilized. **Sales tax paid with the purchase of new cars, boats, airplanes, and home improvements can be used as additions to the IRS-issued tables to calculate the total deduction.**

14. AD VALOREM TAXES

Personal property taxes and real estate taxes are imposed annually by most local governments based upon the "assessed value" of real estate and tangible business property. The "assessed value" generally may not exceed actual value. In many jurisdictions, "assessed value" is far below actual value. The rate of tax varies widely. In Florida it can exceed 3% of assessed value.

15. TAX IMPOSED ON TRANSFER OF APPRECIATED U.S. PROPERTY BY A U.S. PERSON OR RESIDENT ALIEN TO A NON-U.S. ENTITY

The 35% excise tax previously imposed on transfers of appreciated U.S. property by a U.S. person to foreign corporations and/or a foreign partnership, trust or estate **has been repealed. New regulations now generally require the recognition of taxable gain on such transfers** as if the amounts had been sold at fair market value. No built-in gain is recognized on transfers to partnerships if the gain is not allocated to any foreign partner on the later sale of partnership property.

Form 8865 must be filed for certain transfers to foreign partnerships by U.S. persons. Form 5471 is used to report transfers to foreign corporations.

Transfers of property to a foreign trust by a U.S. person must be reported to the Internal Revenue Service on a Form 3520.

16. BRANCH PROFITS TAX ON FOREIGN CORPORATIONS DOING BUSINESS IN THE U.S.

In addition to corporate income tax, a foreign corporation doing business in the U.S. directly (i.e., not through a U.S. corporation) is subject to a second level of tax, the branch profits tax (unless modified or eliminated by treaty as discussed in Question O, 1, b). Absent treaty modifications, the branch profit tax is 30% of the "dividend equivalent amount."

The "dividend equivalent amount" is the amount that could have been remitted to the foreign corporation as a dividend, if the operations had been conducted by a separate corporate entity (in other words, the earnings and profits "effectively connected" with the U.S. operations). The "dividend equivalent amount" is reduced (but not below zero) to the extent the branch profits are reinvested in net assets connected with a U.S. trade or business. The "dividend equivalent amount" is increased to the extent U.S. trade or business net assets have been reduced during the year. The branch profits tax is due at the same time and place as the corporate income tax return and is subject to the same procedural and administrative rules as apply to the income tax liability. However, no estimated tax payments are due with respect to the foreign corporation's branch profits tax liability.

It is sometimes possible to organize the process of "winding-up" the affairs of the foreign corporation by liquidating the activities in the U.S. and distributing all of the assets to the shareholder of the foreign corporation. Such a liquidation, if effected by the end of the fiscal year immediately following a year in which a sale of U.S. assets at a net gain occurs, will be free of branch profits taxes and U.S. withholding taxes only if (a) **there are no current or cumulative U.S. earnings and profits** in the corporation at the time of liquidation; and (b) if the liquid assets available after the sale of the assets meet certain criteria as to the nature of interim investment.

As an alternative, the foreign corporation may be liquidated. If the foreign corporation is liquidated or if the U.S. investments are liquidated under such circumstances, no related corporation may reinvest in the U.S. for three calendar years, or the taxes avoided by the liquidation will become due and payable along with interest and possible penalties.

17. BRANCH LEVEL INTEREST TAX ON FOREIGN CORPORATIONS DOING BUSINESS IN THE U.S.

In order to equalize the treatment of a U.S. branch of a foreign corporation and a U.S. subsidiary, any interest paid by the U.S. branch is "U.S. source income" and is subject to U.S. withholding tax at a 30% rate unless the tax is modified by a specific U.S. tax code or income tax treaty provision.

G Continued

If the branch has an interest deduction allocated to it, under the U.S. Internal Revenue Code rules for allocating income and deductions, in excess of the amount actually paid, this excess is treated as paid to the foreign corporation on the last day of the foreign corporation's taxable year and is subject to a 30% tax unless modified by treaty. Caution: See Question O, 1, e.

H. WHAT TYPES OF INCOME ARE EXEMPT OR DEFERRED FROM U.S. TAX?

The following is a partial list of the most commonly used exempt income or tax deferred income provisions in the U.S. tax law, **in addition to exemptions available to non-resident aliens described in Question E, 1.**

1. Interest on state and municipal bonds is **exempt**. Federal bond interest is taxable by the federal government, but not by states. Any exception to the federal tax is provided for bonds used for higher education. Some state and municipal bond interest is subject to the alternative minimum tax.

2. U.S. corporations generally qualify to exclude dividends from income on three different levels depending on the degree of investment in the corporation. These levels are set at 70%, 80% and 100% exclusion of dividends received from other U.S. corporations.

3. Disability insurance benefits are generally **exempt** (unless premiums paid were tax deducted) as are awards for personal injury.

4. Scholarships are **exempt**.

5. Life insurance proceeds, inherited property, distributions of trust principal, and gifts are **exempt** from income tax to the recipient, though the estate or donor may have to pay estate or gift taxes.

6. Income earned of up to $97,600 outside the U.S. for the performance of services can be tax exempt (See Question M, 8).

H Continued

7. Gain of $250,000 per single person or $500,000 per married couple for the sale of a personal primary residence can be excluded from income. This exclusion cannot be used more frequently than every two years and requires that the property was the principal residence for 2 of 5 years preceding the sale. Gain above this level would be taxable at capital gain rates. Non-resident aliens can rarely use this tax benefit. This exclusion is generally not available to foreign persons selling their U.S. vacation home, but could be very significant to those intending to adopt U.S. tax residency or those for which the U.S. home was their principal residence for 2 of 5 years preceding the sale. Foreign residences may qualify, as may boats used as principal residences.

   Under certain circumstances, a reduced exclusion amount may be allowed when the property has been held for less than 2 of 5 years. These circumstances include change in place of employment, health, or unforeseen circumstances. Treasury regulations define unforeseen circumstances as occurrences such as:

   - death;
   - the cessation of employment as a result of which the individual is eligible for unemployment compensation;
   - a change in employment status that results in the individual's inability to pay housing costs and reasonable living expenses;
   - divorce or legal separation;
   - multiple births resulting from the same pregnancy.

   In these instances, a calculation is made to pro-rate the exclusion amount for the short period of ownership.

8. The American Jobs Act of 2004 created a deduction relating to income attributable to domestic production activities. The U.S. production activities deduction is available to "C: corporations, "S: corporations, partnerships, sole proprietorships, cooperatives, and estates and trusts. Either the taxpayer's taxable income or "qualified production activities income" (QPAI), whichever is less, can be reduced by up to 9%, but is limited to 50% of wages reported on Forms W-2.

   QPAI is equal to domestic production gross receipts reduced by allocable cost of goods sold, directly allocable deductions and a ratable portion of other deductions.

"Domestic production gross receipts" result from the sale, exchange, lease, rental, license or other disposition of:

a. qualifying production property manufactured, produced, grown or extracted by the taxpayer in whole or in significant part in the U.S. (including agricultural products which the taxpayer stores, handles or otherwise processes, but not including transportation activities);
b. any qualified film produced by the taxpayer; or
c. electricity, natural gas or potable water produced by the taxpayer in the U.S.;
d. construction activities performed in the U.S.; or
e. engineering or architectural services performed in the U.S. for construction projects located in the U.S.

Domestic production gross receipts do not include receipts from:

- the sale of food or beverages prepared by the taxpayer at a retail establishment;
- the transmission or distribution of electricity, natural gas or potable water; or
- property that is leased, licensed, or rented by the taxpayer for use by any related party.

Qualifying production property means tangible personal property, computer software, films, tapes, records and similar reproductions. To be a qualified film, 50% of the total compensation relating to the production of the film must be for services performed in the U.S. by actors, production personnel, directors and producers.

The deduction for pass-through entities is determined at the shareholder, partner or similar level by taking into account the proportionate share of QPAI of the entity after the entity has taken into consideration the wage limitation described above.

The concept of what constitutes "manufacturing" or "production" has not been defined in this context which may present a number of planning opportunities.

9. Income earned by controlled foreign corporations may, under certain circumstances, be tax deferred for U.S. shareholders (See Question M, 5, a).

H Continued

10. Generally, gains from condemnations (government taking of property), from involuntary conversions and from exchanges of like-kind business use or investment property can result in deferral of recognition of the gain until the replacement property is sold. If property is condemned or involuntarily converted, replacement property need not be acquired until the end of the third year following the year in which proceeds are first realized. Business use or investment property is exchanged for "like property." There is a possibility to effect a three-way exchange whereby the target property is accepted in lieu of cash within 180 days of the sale. A provision also exists for acquiring the target property 180 days before the sale of the property to be replaced.

11. Certain debt forgiveness income from sales involving seller financing by non-dealers when proceeds from the sale are deferred to future years, all result in the deferral of taxes on the gain to future years. Special limitations on tax deferrals relative to seller-financed sales apply to (a) sales to related parties, (b) sales over $150,000 when installment obligations are pledged or assigned, and (c) when the total of such obligations exceeds $5,000,000. Prior legislation to disallow accrual basis taxpayers from utilizing installment sales has been retroactively repealed.

12. Profits on export sales of U.S. personal property and services outside the U.S. can qualify for reduced or deferred income taxes. The tax can be deferred on the first $10,000,000 of qualified export sales made by an IC-DISC. There is an interest charge described in Question G, 6, a. Even though the FSC has been repealed, there are transitional rules that allow certain FSCs to still enjoy their qualified export sales being subject to tax at a reduced rate (See Question G, 6, b).

13. Pension plans are used to defer income to retirement years. IRA, SEP, Keogh, Profit Sharing, 401K, Defined Benefit, Defined Contribution, and Money Purchase Plans all work to defer income earned from the performance of services from taxation. Roth IRAs offer the opportunity to have tax-free income accumulated in one's retirement account.

14. The cash basis of accounting is available n some instances to defer income taxes. The cash basis of accounting is available for service-type industries rather than sales organizations because the use of inventory for resale will generally require the use of the accrual method. Also, certain entities are not permitted to use the cash basis of accounting. In recent years, "C" corporations (other than qualified personal service corporations) or partnerships with "C" corporations as partners which average more than $5,000,000 in gross receipts have not been allowed to use the cash basis. Any entity required to register as a tax shelter cannot use the cash basis of accounting. However, in general, any business grossing under $1,000,000 can use the cash basis of accounting. Revenue Notice 2001-76 allows the cash basis of accounting to be used by businesses grossing less than $10,000,000 if they are in industries other than mining, manufacturing, wholesaling, retail or information industries.

15. Reporting of taxable income from long-term contracts of companies with under $10,000,000 in average annual revenues and those construction **custom homes** may be **deferred** until the year of completion of those contracts.

16. The **valuation of inventory at LIFO** (last-in, first-out) can **reduce taxable income** below FIFO (first-in, first-out) during periods of inflation.

17. The principal individual tax deductible expenditures allowed by the U.S. are home mortgage interest, real estate taxes, contributions to charities and state income taxes. All are subject to limitations. State and local sales taxes are now also deductible by residents if they elect to deduct this tax in lieu of state or local income taxes. This provision principally benefits residents from states where there is no personal income tax system in place. However, it is important to note that the full benefit of deductions may not be realized by high income taxpayers and by those affected by the "alternative minimum tax" which is expected to affect more than half of all taxpayers in the next several years.

18. Per diem expense allowances for "temporary" work away from a "tax home" (generally for up to a year) are tax free within specified limits. This cannot be used in conjunction with the "income earned outside the U.S. exclusion" described in Question H, 6.

Note: The **alternative minimum tax** may lessen the advantage of some tax deferrals and deductions.

19. Qualified disaster relief payments, including payments to cover reasonable and necessary personal, family, living, funeral, and home repair or rehabilitation expenses, are tax free. Payments from federal, state, or local governments, charitable organizations, and employers to cover disaster related expenses are excluded from income. FEMA reimbursements for taxpayers affected by the recent hurricanes are included in this definition.

I. WHAT ARE THE U.S. TAX EFFECTS OF EXCHANGE CONTROLS IMPOSED BY A FOREIGN COUNTRY WHICH PREVENT THE CONVERSION OF THE FOREIGN CURRENCY INTO U.S. DOLLARS?

Generally, individuals must report their foreign income in terms of U.S. dollars. When foreign income is not readily convertible into U.S. dollars due to restrictions imposed by the foreign country or cannot be converted into other money or property that is readily convertible into U.S. dollars, then the income is considered "blocked." Generally, the taxpayer can defer, including such income in their annual taxable income, until the foreign currency could readily be converted into U.S. dollars.

Deferral is achieved by filing timely an election with a federal income tax return and attaching an information report. The report provides an accounting for the deferred income in the currency of the country that has imposed the exchange control restriction.

I Continued

When "deferrable income" is considered to be "unblocked," the income will be included in the

taxable income of the taxpayer in the tax year in which such exchange control restriction was lifted. The amount shall be translated into U.S. dollars at the appropriate exchange rate for the translation period during which such currency/exchange control restriction is lifted.

J. CAN A U.S. TAXPAYER CLAIM A CREDIT FOR TAXES PAID IN A FOREIGN COUNTRY?

In general, the U.S. tax law permits qualified U.S. taxpayers who pay income taxes in a qualified foreign country to either deduct the taxes from gross income for U.S. purposes or to credit them dollar-for-dollar against the U.S. income tax liability on foreign source income. Foreign taxes paid can be used to offset up to 100% of U.S. taxes on foreign income.

A taxpayer must make an annual election to either use the foreign taxes as a credit against U.S. taxes or to take the deduction against U.S. taxable income. Generally, it is advisable to take a credit against the federal income tax for the amount of income taxes paid. If a credit is claimed, the amount of the foreign taxes may offset, dollar-for-dollar, the U.S. tax due, while a deduction reduces only the amount of income subject to tax. A credit may also be taken even if the taxpayer does not itemize deductions, thus allowing the standard deduction to be taken in addition to the foreign tax credit. The amount of the foreign tax for which credit is allowed is the tax on the profits or income computed by the foreign country's standards.

An individual who elects to utilize the foreign credit must file Form 1116 and attach it to their Form 1040 individual tax form. This filing requirement may be disregarded if foreign source income is comprised of passive income and no more than $300 ($600 if married, filing jointly) is claimed towards the foreign credit.

If the foreign income tax is imposed on the combined income of two or more related persons, i.e., a husband and wife who are jointly and severely liable for the tax under the foreign law, the foreign tax is considered to impose legal liability on each person for the foreign tax attributable to his or her part of the base of the tax. It does not matter who actually pays the tax.

In certain circumstances, a U.S. corporate shareholder which owns 10% or more of a foreign corporation is entitled to an indirect foreign tax credit for foreign taxes paid the by foreign corporations that are "deemed paid" by the shareholder. This indirect credit is available with respect to dividends paid by a qualifying foreign corporation to a qualifying U.S. domestic corporation. U.S. shareholders that are entitled to an indirect foreign tax credit must include the amount of the indirect credit in their income (the "gross-up").

J Continued

Foreign tax credits are not allowed for countries:

1. in which the government is not recognized by the U.S.;
2. with respect to which the U.S. has severed diplomatic relations or does not conduct diplomatic relations;
3. that the Secretary of State has designated as a foreign country that repeatedly provides support for acts of international terrorism.

K. HOW MAY NON-RESIDENT ALIENS STRUCTURE THEIR HOLDINGS USING TRUSTS PRIOR TO BECOMING U.S. RESIDENTS IN ORDER TO REDUCE TAX EXPOSURE AND/OR EXPOSURE TO CREDITORS? (See Caution, Page 1)

1. TRUSTS TO AVOID U.S. TAXES (*THE RULES HAVE CHANGED SINCE 1995*)

In the past, trusts have sometimes been used to reduce or avoid many of the taxes described in Question G. An individual who planned to immigrate to the U.S. would transfer his income-producing assets to an **irrevocable trust prior to becoming a U.S. resident**.

Then, if the trust had the appropriate characteristics, the only U.S. taxes described above which applied to non-U.S. assets were the individual income taxes on payments to the individual, such as payments under an employment agreement with one of the trust-owned companies.

Alternatively, the trust would be structured as a "grantor trust" so as to make the creator of the trust (who would not be immigrating to the U.S.) the party deemed to be taxable on all income. The U.S. beneficiaries, usually children, receive distributions from the trust free of taxes. **This arrangement survived the legislation if the trust creator retains the right to revert the assets to himself without permission of any other non-subservient party (See below).**

However, if a U.S. person becomes an "owner" of any portion of the trust, then that person is taxed on the portion of income he owns whether or not distributed. Additionally, there would be information returns to be filed which are discussed below.

Legislation enacted in August 1996 all but eliminates the use of a foreign trust to avoid U.S. taxes. The new rules, which apply to **trusts created after September 19, 1995**, deny grantor trust status to foreign trusts that have a foreign person as the grantor, with two exceptions:

a. Where the trust may be revoked by the grantor; or
b. Where distributions from the trust during the grantor's lifetime may only be made to the grantor or to the spouse of the grantor.

However, neither of these exceptions will apply where a U.S. beneficiary of the trust has made transfers of property by gift (directly or indirectly) to the foreign person who is the grantor of the trust, unless such gifts were gifts of less than $14,000 per annum and were made while the donor was a U.S. citizen or resident.

U.S. persons who are grantors of property to a foreign trust are required to file an information return to report the transfer. Also, **U.S. beneficiaries of foreign trusts are also required to file information returns that identify the trust, the aggregate amount of distributions received from the trust during the year and other information necessary to determine the taxability of such distributions.** This information is reported on Form 3520. If insufficient information is provided, the Internal Revenue Service will now have the authority to treat all such distributions as an "accumulation distribution" that is fully taxable and subject to the non-deductible interest penalty.

Loans by a foreign trust to a U.S. beneficiary or grantor will usually be treated as a distribution to the U.S. beneficiary or grantor, which requires them to file Form 3520 mentioned above.

The new legislation puts **foreign grantors** in the same position **if they become U.S. residents within 5 years of contributing property to a foreign trust.** The foreign grantor is deemed to have transferred such property to the trust on the date that the foreign grantor became resident in the U.S. Therefore, after establishing residency, the grantor will, in most cases, become taxable on the income of the trust, and, in any event, will be required to file an information return with respect to the trust. Form 3520-A is required to be filed by the trust where there are U.S. grantors to a foreign grantor trust.

The Internal Revenue Service has been given the power to re-characterize a gift or bequest from a foreign partnership or foreign corporation that results in a foreign grantor trust being created. The use of such entities as a conduit of the individual grantors will be subject to **re-characterization of transfers as income**.

In addition to the re-characterization of gifts, a penalty of up to 35% of the gross reportable amount is assessed against the person required to file the information return if they **fail to comply** with the reporting requirements listed above.

The new rules do not impose additional reporting requirements directly on offshore trustees, but the new reporting requirements imposed on grantors and beneficiaries require information that can only come from the trustee and will obviously increase the administrative burden and expense in order to comply.

A further word of caution: Before becoming a U.S. resident, it may become necessary to become a resident of an interim tax-haven country prior to transferring assets into trust (or into corporate ownership or by gift – see Question M) since your present country of residence may impose taxes on such transfers while you are a resident of that country. The 5-year rule described above may, however, make this planning technique impractical.

2. ASSET PROTECTION TRUSTS

Trusts are also commonly used to protect assets from the grantor's creditors. An "asset protection trust" must be formed **by a solvent grantor before creditors' claims have arisen**. Otherwise, the transfer will be vulnerable to charges of fraudulent conveyance. A foreign trust may be more effective than a U.S. trust for asset protection since a creditor's claim must then be pursued in a foreign jurisdiction. A creditor's attempt to teach the assets of a foreign asset protection trust will most likely be based on an argument that the grantor retained an interest in the assets which is reachable by the creditor under local law. Therefore, **it is imperative that the grantor retains as little interest in and control over the transferred assets as possible.** In order to successfully assert that the grantor has not retained an attachable interest, someone else must have a superior interest in the trust (See Question L, 2).

L. CAN GRANTORS GIVE THEIR ASSETS TO TRUSTS AND STILL BENEFIT FROM THEM? (See Caution, Page 1)

The following descriptions generally pertain to trusts created prior to September 19, 1995 and more than 5 years prior to the grantor becoming a U.S. resident (See Question K).

1. TWO TYPES OF STRUCTURES ARE IN COMMON USE

One method is to irrevocably grant to an "**adverse party**" trustee or trust protector a **general power of appointment** over the trust income and assets. The holder of a **general** power of appointment can distribute trust assets at his sole discretion, **even to himself**. The grantor of the trust can give a **general** power of appointment over the trust to anyone he chooses to designate, **but the holder would normally be someone the grantor can trust**. Because the holder of a **general** power of appointment can use trust income or principal for his own purpose, the holder is an "**adverse party**," which is defined as a person whose own interest would be decreased by any use of income or principal by the grantor. Because the holder of a **general** power of appointment is an "adverse party," the grantor is able to designate a **related person(s)** (other than a spouse) as the holder, e.g., parents, children, siblings or persons normally considered subservient to the grantor, such as employee or agent, **without the rights of the holder being deemed attributable to the grantor**.

The theory of such an arrangement is that any distribution of trust assets to the grantor would be adverse to the holder's interest; therefore, the grantor would not be considered to have retained any of the rights which were vested in the holder of a **general** power of appointment. Of course, the clear problem is that the grantor loses control of his assets by placing them at the disposal of someone else.

Another method recommended by some advisors is to irrevocably grant to a "**non-adverse party**" trustee or trust protector a **limited** power of appointment over the trust income and assets. The limitation prohibits distribution to the "holder" of the power of appointment. This makes the "holder" a "**non-adverse party**." The theory of such an arrangement is that any distributions, including one to the trust grantor, first requires the consent of the trustee, a "**non-adverse party**;" therefore, the grantor would not be considered to have retained any of the rights vested in the holder of the **limited** power of appointment. Of course, the grantor/spouse cannot be a named beneficiary.

Further, **no "related party"** who is not an "adverse party" as described above, can be named as the holder of the **limited** power of appointment since such power would be attributed to the grantor. **Here again, the grantor loses control of his assets**.

We are concerned that either structure may fail the test of whether the grantor/spouse is in "control" of the trust or is a trust "beneficiary" since, in the instance of distributions being made in the first case, the "adverse party" trustee is "freely" giving what are now, effectively, his own assets to the grantor and in the second case, only the "consent" of a non-adverse party must be required in order for there to be a distribution. The appearance of a "sham" arrangement implying some sort of "side agreement" or other influence may be extremely difficult to overcome when the question is asked, "Why was the distribution made to the grantor?"

An additional method commonly used to derive benefit from assets under either trust structure is through the creation of a corporation, which is owned by a trust. The trust grantor is then employed by the company at arm's-length rates as an employee or under a consulting contract or employment agreement. Payments are income to the recipient and deductible to the corporation. Payments must be reasonable in amount and be ordinary and necessary business expenses of the corporation. This arrangement must be structured in a matter which avoids giving the trust grantor effective control over trust assets (such as having the trust grantor as the chief [or sole] corporate executive and/or director). This is of particular concern if the stock in the corporation is the trust's only or principal asset. If the trust grantor retains sufficient control over the corporation to determine the amount of payments his is to receive, the arrangement may imply "control" of the trust by its creator and the trust grantor will be taxable on all trust income.

2. INCOME TAX CONSIDERATIONS OF AN "ASSET PROTECTION" TRUST

Any holder of a general power of appointment discussed in the preceding paragraphs should probably be a non-resident alien since the mere existence of the **general** power of appointment makes trust income taxable to the holder. A U.S. citizen or resident alien would be subject to U.S. income and estate taxes, even if the **general** power of appointment is not exercised. The grantor's spouse should not be given a **general** power of appointment even if he or she is a non-resident alien, since the rights of the spouse are attributable to the grantor.

Finally, extreme care should be taken to avoid the appearance of control or an enforceable beneficial interest by the grantor/spouse over the trust assets. It must not exist, in fact, or the grantor will be deemed to be the owner of the trust assets for U.S. tax purposes.

3. AN ALTERNATIVE TRUST STRUCTURE TO INVEST IN THE U.S. – PRE-SEPTEMBER 15, 1995 TRUSTS AND THOSE CREATED MORE THAN 5 YEARS BEFORE BECOMING A U.S. RESIDENT

An alternative structure to provide funds for use in the U.S. is an irrevocable foreign trust that is funded with a combination of contributions and loans. In this way, a foreign investor does not relinquish control over the loan funds. The trust should have an independent trustee, the loan must have "arms-length" terms and the trust grantor must not retain prohibited powers over the trust assets. If all formalities are observed, the trust should be recognized for U.S. federal income tax purposes. The trust would be taxed on its U.S. income net of interest paid. (See Question O, 1, e for a guideline as to a statutory debt-to-equity ratio for corporate offshore financing among related parties.) Interest payments to the non-U.S. grantor should provide an annual income stream, which would be excluded from U.S. tax as "portfolio" interest income. Of course, once the grantor becomes a U.S. resident, he is taxed on the income stream.

M. OTHER THAN TRUSTS, WHAT CAN AN INDIVIDUAL DO BEFORE BECOMING A U.S. RESIDENT TO REDUCE U.S. TAXES? (See Caution, Page 1)

1. GIFTS BEFORE IMMIGRATION TO U.S.

Gifts of income producing property to children prior to becoming a U.S. resident can serve to reduce taxes although the children, if U.S. residents, will be taxed in the U.S. on income from assets owned by them. Consideration should also be given to funding sufficient amounts to life insurance trusts in order to meet future premium obligations. These transfers to life insurance trusts are considered non-taxable gifts.

As mentioned in Question F, 2, gifts of **intangible** assets between non-resident aliens are not subjected to the gift tax. This includes gifts of shares of stock in a U.S. corporation.

2. VARIABLE ANNUITIES

Variable annuities with a life insurance feature which are purchased by exchange of an individual's assets (such as portfolio investments) appear to be growing in popularity as an alternative to trusts.

3. SALES BEFORE AND AFTER IMMIGRATION TO U.S.

Any gains on sale of assets (including corporate liquidations and exercise of most stock options) by a resident alien **after immigration** to the U.S., no matter where the assets are located or where the options were earned, are generally taxed in the U.S. The amount subject to tax is the difference between the proceeds of sale or liquidation and the original cost (regardless of the value at the time of immigration).

For this reason, it is often desirable to **sell appreciated property**, **liquidate appreciated corporations** and to **exercise stock options** or to sell them (or other properties) **prior to the time of immigration**. This would avoid a U.S. income tax on the sale or liquidation.

Qualified losses incurred **after** immigration may be used to offset taxable gains. **For this reason, it may be best to delay the sale or liquidation of investments on which a loss will be realized until after immigration**.

Under the principal residence exclusion, a person is generally entitled to exclude from income $250,000 of gain ($500,000 for a couple filing jointly) on the sale of a principal residence within 2 years after moving to the U.S. Additionally, immigration to the U.S. due to a change of employment or health reasons will allow a pro-rated portion of the exclusion to the immigrant to avoid some gain if the above regulations cannot be met. Other circumstances which allow for a pro-rated exclusion to be used are discussed in Question H, 7.

Payments received under an installment sale which was entered into prior to the individual becoming a resident of the U.S. are exempt from U.S. taxation.

4. INHERITED PROPERTIES

If a U.S. resident acquires property anywhere in the world through inheritance from the estate of a foreign decedent, the heir's cost of the property for purposes of determining taxable gain on a resale is generally the fair market value in the estate of the decedent. Thus, a sale of inherited property soon after the death of the foreign owner would result in very little U.S. capital gains tax being imposed on the sale. There would be no U.S. estate tax on such an inheritance except to the extent the inherited property was U.S. property. An exception to the "step up" of basis may occur where the property acquired from a decedent was a function of the form of ownership such as holding property as a joint tenant with right of survivorship and the property was not includible in the U.S. gross estate.

Community property rules may also affect the general rule described above but in favor of the taxpayer. If the decedent is a spouse from a community property jurisdiction, the surviving spouse may be entitled to a "stepped-up basis" of the entire property rather than merely half, even if the entire property was not including in the U.S. gross estate of the decedent.

5. CONTROLLED FOREIGN CORPORATIONS (CFCs) AND CONTROLLED FOREIGN PARTNERSHIPS (CFPs)

a. Controlled Foreign Corporations

If a foreign corporation is controlled directly or indirectly by a U.S. person or entity (including resident aliens), then each such U.S. shareholder must provide the U.S. with full financial details of that corporation. A resident U.S. shareholder owning more than 10% of the total combined voting stock may be taxable on corporate income (even if not distributed) under the "controlled foreign corporation" rules.

A foreign corporation is defined as a "controlled foreign corporation" (CFC) if U.S. shareholders, each owning 10% or more of the shares collectively, own more than 50% of the corporate stock (either by voting power or value of stock). **Certain income earned by such corporations, even if undistributed, may be taxable to U.S. shareholders as if it had been distributed.** This undistributed but taxable pro-rata share of income is labeled "Subpart F Income." Note: Under existing law, deemed income inclusions from CFCs (such as Subpart F Income) are not dividends and would not be eligible for the reduced tax on dividends described in Question G, 12.

This rule particularly applies to foreign corporations, the principal income of which is (a) **passive income from investments (dividends, interest, royalties, rents and annuities) and from real estate**, and/or (b) **trading or service income from activities involving a related party and** (as to purchase or sale of products) the products are produced outside the country of incorporation and are purchased or sold for use outside that country; and (as to income from **services**) the **services** are performed outside the country of incorporation.

If a CFC invests in U.S. assets or has more than 25% of its assets invested in passive assets, taxable distribution of income which is otherwise not regarded as Subpart F income, will be **deemed** to have been made to its U.S. shareholders. **Thus, divestiture of control prior to becoming a U.S. person may be desirable.** Legislation enacted in 2004 creates two exceptions to the definition of U.S. assets. U.S. assets do not include securities acquired and held by the CFC in the ordinary course of its trade or business as a dealer in securities or obligations issued by unrelated non-corporate U.S. person. Deposits with U.S. banks are also not considered U.S. assets.

If Subpart F status can be avoided and the income is retained in the CFC, taxability to the U.S. shareholder can be deferred until sale of the corporation or distribution to the shareholder. Gain on the sale of stock of a CFC that is treated as a dividend of the Internal Revenue Code may be eligible for the reduced rate of tax described in Question G, 12.

U.S. persons who are in control of a foreign corporation need to file the information on Form 5471 or face increasingly severe penalties. A penalty of $10,000 may be incurred for failure to comply with these filing requirements, along with a maximum fine of $50,000 for continuing non-compliance. Persons failing to report all Form 5471 information when prescribed also may be subject to a reduction in his or her credit for foreign taxes paid, up to 100%.

b. Controlled Foreign Partnerships

The rules for taxation of U.S. partners in foreign partnerships are identical to those for partners in U.S. partnerships. However, it should be noted that special rules apply to partnerships with U.S. partners and certain transfers of interests in controlled foreign partnerships by U.S. citizens or residents. Reference Question N, 3 for filing requirements.

6. FOREIGN PERSONAL HOLDING COMPANIES

The American Jobs Act of 2004 repealed the foreign personal holding company rules. Under prior law, divestiture of control **prior** to becoming a U.S. resident was previously desirable to avoid classification of the corporation as a "foreign personal holding company." Previously, if fewer than six U.S. individuals, **including resident aliens**, owned more than half of a foreign corporation's stock and 60% or more (50% or more in subsequent years) of the foreign corporation's income was passive investment income, the U.S. shareholders used to be taxed on the income of the foreign corporation even though it had not been distributed to them.

7. PASSIVE FOREIGN INVESTMENT COMPANIES (PFIC)

Any foreign corporation with (a) 75% or more of its gross income as passive income or (b) at least 50% of the average value of assets consists of assets that produce or are held for the production of passive income is a Passive Foreign Investment Company (PFIC). Passive income does not include rents and royalties derived in the active conduct of a trade or business and which is received from unrelated persons. Unless a U.S. shareholder of a PFIC elects to be taxed currently on his share of PFIC earnings, he is taxed as ordinary income when there is a distribution or he disposes of the investment.

8. EMPLOYMENT OUTSIDE THE U.S.

It is now possible for a resident alien, under some circumstances, to work for compensation outside the U.S. and exempt up to $97,600 for 2013, **plus certain housing expenses, from U.S. taxation. A tax return must be filed to claim the exemption, along with form 2555.** Under certain circumstances, late filed elections are allowed to claim the exclusion. **If the alien plans to become a green card holder, but works outside the U.S., this tax exemption could be quite useful.**

To qualify for the exclusion, the resident alien must 1) actually live and work outside the U.S. and during 12 consecutive months must be physically present in one or more foreign countries for 330 full days OR 2) be considered a "bona-fide" tax resident of a foreign country. NOTE: Taxpayers residing in certain high-cost jurisdictions are entitled to larger housing exclusion amounts.

9. PLANNING FOR SPOUSES WITH DIFFERENT TAX RESIDENCES

There are instances where the U.S. tax residence of one spouse is different than the other spouse for U.S. income tax purposes. For U.S. income tax planning purposes, this is ideal where only one spouse works mainly abroad while attending to a home country business interest.

If this spouse monitors his/her presence in the U.S. so as not to exceed the presence described in Question B, then it is possible for the income earned as well as owned by this spouse to be free of U.S. income tax. The other spouse's presence in the U.S. is more substantial with this spouse's assets and income purposely less in amount that that of the U.S. non-resident spouse. Ideally, little to no U.S. income tax is paid by this spouse.

This type of planning is ideal for couples who immigrate from jurisdictions that do not have community property rules in place. Such rules generally provide that all of the marital property of the couple is equally owned by each spouse and, therefore, the income arising from this property is to be equally reported between the spouses. Marital property under the community property rules generally include property acquired during marriage while domiciled in a community property jurisdiction and property that cannot be identified as separate property. Community property income arises from community property and can include wages earned during marriage (regardless of who earned the wages) and real estate income from property treated as community property.

Community property generally does not include property acquired prior to marriage, inherited property, property purchased from separate funds, or income earned while domiciled in a non-community property jurisdiction.

Community property rules should be carefully examined if emigrating from or moving into this type of jurisdiction. See list of community property states in the U.S. at Question F, 3, a.

For instance, there is some relief for "mixed" couples emigrating from a community property regime. If a U.S. non-resident spouse earns income outside the U.S. and also solely owns the home business interest overseas, then it is possible that the income from the business as well as the wages will not be attributable to the U.S. resident spouse as long as this spouse does not exercise substantially all of the management and control of the trade or business in question. There are additional planning opportunities that can override certain traditional community property rules to reduce potential U.S. tax consequences.

N. ONCE A PERSON BECOMES A U.S. TAX RESIDENT, WHAT MINIMUM FILING REQUIREMENTS ARE REQUIRED BY THE U.S.?

1. FOREIGN INCOME AND GAINS

Form 1040 – Annual income tax return reporting worldwide income and gains from all sources is reportable to U.S. and subject to U.S. income taxes (less credit for foreign taxes paid or accrued).

Who must file?

For 2012, the filing thresholds are as follows:

	Under 65	Over 65
Single	9,750	11,200
Married Filing Jointly	19,500	21,800
Married Filing Separately	3,800	3,800
Head of Household	12,500	13,950

2. RELATED FOREIGN CORPORATIONS

Form 5471 – Information Return of U.S. Person With Respect to Certain Foreign Corporations. NOTE: In an effort to increase the compliance, the IRS has announced that it intends to audit all Form 5471 (and 5472) filings pertaining to withholding matters. Taxpayers should ensure compliance with timely filing of all appropriate forms.

a. Who must file?

- (Category 1 filer) This filing requirement has been repealed for tax years beginning after December 31, 2004.

- (Category 2 filer) U.S. citizen or resident officer, director who has acquired at least a 10% ownership interest in a foreign corporation or an additional 10% ownership interest in the foreign corporation.

- (Category 3 filer) A U.S. person who acquires stock in a foreign corporation that meets the 10% stock ownership requirement for the corporation or a U.S. person who disposes of sufficient stock in the foreign corporation to reduce his or her interest to less than the 10% ownership requirement.
- (Category 4 filer) Any U.S. person who owns more than 50% of the total combined voting power of all classes of stock entitled to vote or more than 50% of the value of all classes of stock in the corporation for an uninterrupted period of at least 30 days during the annual accounting period of the foreign corporation.

b. Information Required

The information that is to be reported depends on what category(s) the filer falls under. In addition to providing the foreign corporate name, address, and taxpayer identification number, below is a highlight of some of the reporting requirements.

- Constructive ownership of corporate ownership, disclosure of U.S. shareholder information.
- Information on the classes of stock issued by the corporation as well as information on preferred stock.
- Disclosure of U.S. officers and directors of the foreign corporation.
- Information surrounding the purchase or disposition of foreign corporate stock.
- Income statement and balance sheets.
- Historical earnings and profits information as well as for the current year.
- Disclosure of related party transactions.
- Summary of shareholder's income from the foreign corporation.

If the corporation is substantially inactive during a tax year, then there are provisions available to substantially reduce the reporting requirements.

3. FOREIGN PARTNERSHIPS

Form 8865 – Information Return of U.S. Persons With Respect to Certain Foreign Partnerships. The Internal Revenue Service has issued final regulations to require a U.S. person that transfers property (including cash) to a foreign partnership in exchange for a partnership interest to report the transfer on Form 8865.

a. Who must file?

- (Category 1 filer) Any U.S. person who owns more than 50% of the (i) the capital interest in the partnership, (ii) the profits interest in the partnership, or (iii) in the deductions or losses of the partnership.

- (Category 2 filer) A U.S. person who at any time during the tax year of the foreign partnership owned a 10% or greater interest in (i) the capital interest of the partnership, (ii) profits interest in the partnership, or (iii) deductions or losses of the partnership while the partnership was controlled by U.S. persons owning at least 10% interests.

- (Category 3 filer) A. U.S. person who contributed property to the partnership in exchange for an interest in the partnership if that person either (i) owned, directly or indirectly, at least a 10% interest in the partnership, or (ii) the value of all property transferred by the U.S. person, including the value of property transferred by related parties, within a 12-month period ending on the date of transfer exceeds $100,000.

- (Category 4 filer) A U.S. person who acquires or disposes of a foreign partnership interest where (i) the U.S. person acquires enough of an interest to gain at least 10% of an interest (e.g., from 9% to 11%) after the acquisition or has increased the interest by an additional 10% (e.g., 11% to 21%), or (ii) the U.S. person disposes enough of an interest to fall below owning at least 10% (e.g., from 11% to 8%) or has decreased the interest by at least 10% (e.g., from 21% to 11%).

There are certain exceptions to filing. For instance, if there are multiple Category 1 filers, then only one U.S. person may file as long as the person is a holder of a capital or profits interest. Additionally, if a Category 1 or 2 filer is required to file because the person is considered to constructively own the stock and is not a direct owner, the individual is not required to file as long as the ultimate direct owners file Form 8865.

b. <u>Information Required</u>

The information that is to be reported depends on what category(s) the filer falls under. In addition to providing the foreign partnership name, address, and taxpayer identification number, below is a highlight of some of the reporting requirements:

- Constructive ownership of partnership interest, partner and affiliate information.
- Income statement and balance sheets.
- Capital gains and losses.
- Partners' share of income, credits, deductions, etc.
- Reconciliation of book income with taxable income.
- Analysis of partners' capital accounts.

Failure to file Form 8865 can result in monetary penalties and a reduction in foreign tax credits. A $10,000 penalty is imposed for each failure to file a Form 8865. This amount is increased by $10,000 for each 30-day period in which the failure to comply continues beyond 90 days after receiving written notice from the Internal Revenue Service. The maximum additional penalty is limited to $50,000 per failure. A reduction in foreign tax credits can reach a maximum of $10,000 or the gross income of the foreign partnership for the tax year in which the failure occurs, reduced by the monetary penalty.

Form 8865 is filed with the U.S. person's individual income tax return.

4. FOREIGN BANK & FINANCIAL ACCOUNTS AND CURRENCY TRANSACTIONS

Form TDF 90-22.1 – Report of Foreign Bank and Financial Accounts

We cannot overstate the importance of recent developments in this area. IRS made that enforcement of the TDF 90-22.1 reporting requirements a high priority and offered the Offshore Voluntary Disclosure Initiative (OVDI) and Offshore Voluntary Disclosure Program (OVDP) for non-compliant taxpayers to report their previously undisclosed foreign financial accounts. More details on these "amnesty" programs below.

Who must file?

There are severe penalties for non-willful and willful violations of account reporting requirements.

Each person who has a financial interest in or signature authority or other authority over bank, securities or other financial accounts in a foreign country aggregating in excess of $10,000 must report such accounts annually. Form TDF 90-22.1 requires that each account be disclosed annually with the financial institution's name and address, account number, type of account, and maximum value at any point in the year.

A civil penalty of up to $10,000 may be imposed against any person who violates the reporting requirement (whether willful or not). This penalty may be waived under certain conditions.

The Act has increased civil penalties that may be imposed for willfully failing to file this form. Civil penalties imposed for willfully failing to file the form amount to the greater of $100,000 or 50% of the transaction or account value.

In the wake of the UBS scandal, the Treasury Department offered an amnesty program for individuals in non-compliance with TDF 90-22.1 filings for years 2003-2008. Treasury offered a 6 month window (March 23 through September 23, 2009) for non-filers to submit their forms and pay penalties under a reduced penalty regime. An extension was allowed under IRS Notice 2009-62 until June 30, 2010 only for filers reporting signature authority, not a financial interest, in a foreign account.

The Hiring Incentives to Restore Employment Act (HIRE Act) signed into law on March 18, 2010 expands TDF 90-22.1 reporting requirements to individuals with an interest a "specified foreign financial asset" if the aggregate value of all such assets is greater than $50,000 during the year. "Specified foreign financial assets" are: (1) depository or custodial accounts at foreign financial institutions, and (2) to the extent not held in an account at a financial institution, (a) stocks or securities issued by foreign persons, (b) any other financial instrument or contract held for investment that is issued by or has a counterparty that is not a U.S. person, and (c) any interest in a foreign entity.

The HIRE Act also provides that a 40% penalty is imposed on any understatement attributable to an undisclosed foreign financial asset for tax years beginning after Mar. 18, 2010. This penalty is assessed in addition to the failure to file penalty.

On June 26, 2012, the IRS announced a Streamlined OVDP program for low-risk taxpayers. This Streamlined program was designed for US taxpayers living abroad who have little or no tax due in the US and have been compliant on their tax filings in their home countries.

Form TDF 90-22.1 is due June 30th of each year following the year reported on. Effective July 1, 2013, all Forms TDF 90-22.1 must be electronically filed.

N Continued

U.S. Customs Form 4790 – Report of International Transportation of Currency or Monetary Instruments

Who must file?

The U.S. Government requires that each person must declare to U.S. Customs each transfer **into or out of the U.S**. of more than $10,000 in value of monetary instruments. This includes currency, U.S. or foreign coins, traveler's checks, money orders, negotiable instruments, and investment securities in bearer form. This applies to U.S. and non-U.S. currency. An exception to reporting is allowed for transfers of funds through normal banking procedures which does not involve the physical transportation of currency or monetary instruments.

Failure to comply can result in civil and criminal penalties, including seizure of the currency or monetary instruments.

Individuals who receive currency or other monetary instruments in the U.S. in excess of $10,000 must file Form 4790 within 15 days after receipt with the Customs officer in charge at any port of entry or departure or by mail with the Commission of Customs. For travelers carrying currency or other monetary instruments, the form shall be filed at the time of entry into the U.S. or at the time of departure with the Customs officer in charge. For shippers or mailers of the currency or other monetary instrument that does not accompany the individual entering or department the U.S., Form 4790 may be filed by mail on or before the date of entry, departure, mailing, or shipping with the Commission of Customs.

Form 8300 – Report of Cash Payments Over $10,000 Received in a Trade or Business

Who must file?

The receipt of "cash" of more than $10,000 in one transaction, or in two or more related transactions, in the course of the recipient's trade or business must be reported on an information return to Internal Revenue Service **by the recipient.** This rule applies whether or not the receipt is income in the trade or business.

For this purpose, cash includes the currency of the U.S. and any foreign country. Also included are cashier's checks, bank drafts, traveler's checks or money orders under $10,000 and received in (i) a designated reporting transaction, or (ii) any transaction in which you know the payer is trying to avoid the reporting of the transaction on Form 8300. A designated reporting transaction is the retail sale of consumer durables (tangible property suitable for personal use other than land or buildings lasting at least one year with a sales price of more than $10,000), a collectible, or travel or entertainment if the total sales price of all items sold for the same trip or entertainment event is more than $10,000

Payments with bank drafts, cashier's checks, traveler's checks, or money orders for amounts over $10,000 need not be reported since these are reported by banks. Payments with personal checks, regardless of the amount, are also exempt from reporting as the transactions are reported by banks.

Banks, utilizing U.S. Financial Crimes Enforcement Network Form 104 (Replacing Form 4789), report to Internal Revenue Service on Cash Transaction Reports (CTRS) information on individuals receiving or depositing cash of $10,000 or more per transaction and short-form CTRS on checks cashed exceeding $2,500. In addition, casinos are required to obtain identifying information for persons involved in all casino related transactions of $3,000 or more during a gaming day. This includes purchases or redemption of chips and wagers of $3,000 or more.

Form 8300 is due on the 15th day following the receipt which totaled $10,000 or more or aggregate thereof. The USA Patriot Act of 2001 has increased the scope of the laws enforcing such filing measures to aid in the fight against terrorism.

5. OTHER CIRCUMSTANCES WHICH REQUIRE FILING

Beyond the above described reporting requirements, once a person becomes a U.S. tax resident, numerous transactions or events involving the new tax resident will cause reporting and/or tax requirements.

These transactions or events include, but are not limited to:

- sales or trades of U.S. or foreign assets;
- creation, liquidation, distribution from, or transfer to trusts or corporations;
- employment or performing services for corporations;
- engaging in a trade or business;
- employing anyone to perform service such as housekeeper or other employee;
- receipt of interest, dividends or other income from any source – worldwide;
- gifts;
- death.

O. HOW MAY NON-RESIDENT ALIEN INDIVIDUALS AND CORPORATIONS BEST PROTECT THEMSELVES AGAINST U.S. TAXES IF THEY DO NOT INTEND TO BECOME RESIDENT ALIENS? (See Caution, Page 1)

1. HOW TO HOLD INVESTMENTS IN U.S. REAL ESTATE

a. Holding title to real estate – should ownership be held by a U.S. subsidiary of a foreign corporation or directly as an individual?

Before a comparison of asset structure begins, it is important to understand that **all gains on sales** or other taxable **dispositions of U.S. real property interests (USRPIs) are taxable by the U.S.** This tax is unavoidable, regardless of the asset structure. However, **proper planning can avoid** the imposition of **U.S. estate taxes** on such assets.

Ownership of U.S. real estate by a U.S. subsidiary of a foreign corporation protects the beneficial owner against **U.S. estate taxes and U.S. branch profits tax; it provides for non-disclosure of beneficial ownership in the public records; it eliminates U.S. withholding tax** on a subsequent sale of the property, and generally provides a **better protection against legal liability of the ultimate beneficial owner** with respect to the investment.

Under present law, newly acquired and existing U.S. real property interests, as well as U.S. real property and real property partnership interests with minimal appreciation in value generally should be purchased by or conveyed to a U.S. corporation which in turn is owned by a foreign corporation. The shares of the foreign corporation **will escape U.S. estate tax upon the demise of the foreign shareholder**, since the shares of a foreign corporation are not U.S. situs property.

Caution: Recent aggressive policies initiated by Internal Revenue Service have acted to include the value of U.S. real property in the estate of a non-resident decedent where a conveyance during the lifetime of the decedent to a trust or foreign corporation was held **not to be for "full and adequate consideration."** In the past, the conveyance of U.S. real property or the stock of a U.S. corporation holding real property (USRPI) in exchange for shares of foreign corporation was considered "full and adequate consideration." This position may now be open to attack by Internal Revenue Service.

It has been suggested that the **actual transfer of cash in consideration for the USRPI would be preferable.** If this cannot be done for currency restriction or liquidity concerns, **payment might be effected by use of a note payable from the foreign corporation.** This note could then be paid at a later date. However, care should be taken that the obligation not be that of a U.S. corporation or other U.S. entity, since inclusion of the obligation in the non-resident's taxable U.S. estate would result.

Holding U.S. property by a U.S. subsidiary of a foreign corporation versus holding the property individually better protects against the U.S. estate tax despite the aforementioned policies of the Internal Revenue Service. An individual would not be fully protected from the U.S. estate (death) taxes if the U.S. real property interests were held individually. U.S. estate taxes would be imposed on the value of the holdings that exceed $60,000 (but see discussion of non-recourse debt in Question F, 4, a). This tax would be imposed even if the property is held by a U.S. corporation, which is owned by a foreign person.

Ownership of U.S. real estate by a U.S. subsidiary of a foreign corporation also protects the beneficial owner against the branch profits tax under current law. The branch profits tax would apply if the ownership of the property is in the name of the foreign corporation and the U.S. "operation" is thus conducted as a branch of the foreign corporation (without using a U.S. subsidiary corporation to hold the property). Unless treaty protection against branch profits tax is available, exposure to branch profits taxes will result. Generally, a separate U.S. corporation should hold each USRPI. This reduces exposure to "branch profits" taxes when a property is sold.

Note: There is a proposal to impose the branch profits tax under the foreign parent/U.S. subsidiary scenario on the occasion of liquidations, which is now tax exempt. If this change in tax law is made, the tax on the gains from such structures could increase from a maximum of 40% to a maximum of 58% - 60%.

If a non-resident individual holds title to the property, the branch profits tax described above does not apply to gains on sale of the property. The individual enjoys a much lower tax (20% rate) due on gains on sale of the property. Also avoided are annual corporate charges and a need to file a tax return in the U.S. unless an individual rents or sells the property.

Anonymity is another principal reason for many people holding property in the name of a corporation rather than having their own names in the public records. No public registry of owners of shares is published in the U.S., whereas the owner of real estate is a matter of public record in courthouses throughout the U.S. The Internal Revenue Service is notified of ownership of shares of a U.S. corporation, which is why foreign holding companies are often used to own the shares of the corporation. This asset structure also becomes useful when a request for refund of taxes withheld on the sale of property is made. In order to request a refund, the owner of the property must obtain a U.S. federal identification number.

If the record owner is a corporation, the corporation is identified and not the ultimate beneficial owner. If the owner is an individual, then obtaining of the necessary identification number will require furnishing the Internal Revenue Service with full disclosure of personal identification information including copies of passports and birth and foreign residence information. The U.S. government does send information on foreign ownership to treaty partner countries, which is why many people choose to have the shares of the U.S. subsidiary held by foreign corporations which are formed in neutral or tax-haven countries.

The protection of anonymity and the other benefits provided by having the U.S. property held by a U.S. subsidiary of a foreign holding company does come with a price. The **corporate** tax rate on gains from the sale of the asset is 35% maximum federal capital gains tax plus the applicable state corporate Income tax. For instance, if a corporation were to sell property situated in Florida, a maximum corporate income tax of 40.5% could be realized if the maximum **federal long-term capital gains rate** of 35% (See Question G, 10) and the Florida corporate income tax of 5.5%* are imposed. This tax rate is significantly higher than the comparable federal and applicable state capital gains tax rates for an **individual** who owns the property in his own name. For instance, there would be **maximum federal long-term capital gains rate of only 20% for sales taking place, or capital gain payments received after December 31, 2012** (See Question G, 10) if the sale involves property in Florida. Also, because the State of Florida does not have an individual income tax, no state income taxes would be due on the sale by an individual.

*See Tables P-1 and P-2 for other state corporate and individual income tax rates.

Another advantage to holding U.S. property by a U.S. subsidiary of a foreign corporation is that this structure is exempt from withholding taxes on sales of real estate. Non-resident owners of U.S. real estate are generally subject to a 10% withholding tax on sales of U.S. real estate unless the property is worth less than $300,000 and it is to be used by the buyer as a primary residence. One might infer that properties under $300,000 in value could safely be held by individuals, without involving a complex corporate holding arrangement. However, when one buys such property, one never knows if the future buyer will qualify the seller for this "residence exemption." Moreover, the other advantages of the more complex holding arrangement are still of importance to many foreign investors for the other reasons cited.

The paragraphs above are intended to allow the foreign investor to weigh the options when determining ownership structure. **There is not one correct answer for all non-resident individuals regarding the ownership structure of U.S. property. For those individuals who choose to own U.S. property through a U.S. subsidiary of a foreign corporation, the following paragraphs should also be considered.**

The stock of a U.S. corporation that holds U.S. real estate is, by definition, a USRPI. **A distribution or sale of the U.S. stock by the foreign corporation or liquidation of the U.S. corporation will result in taxable gain to be recognized, much as if the real estate itself had been sold.**

If the USRPI is already owned by a non-U.S. individual and has appreciated in value, special problems may prevent the tax-free transfer of the USRPI to a foreign corporation or to the U.S. subsidiary of the foreign corporation. For a tax-free transfer in this case, the foreign corporation must be incorporated in a qualified treaty country. Then, when a USRPI is conveyed from a foreign corporation to a U.S. subsidiary, the foreign corporation must make an election to be taxed like a domestic (U.S.) corporation under U.S. IRC 897(i). This special election allows the foreign corporation to be exempt from withholding requirements under the Foreign Investors Real Property Act (FIRPTA) on that conveyance, but does not apply to any other provision of the tax code. **If the foreign corporation is in a country other than a qualified treaty country, the transfer of the USRPI to the foreign corporation or its U.S. subsidiary will be subject to tax under FIRPTA.**

Note: Some tax advisors predict that Congress may resurrect a tax proposal that failed to pass Congress in 1992 but came close to becoming law at that time. The proposal would impose a capital gains tax on any gain realized from a sale or liquidation of a U.S. corporation by a 10% or more foreign owner if that corporation has been held for any part of five years by the foreign owner prior to liquidation. The start date for measuring the five-year holding period, as was proposed in 1992, was for such ownership existing on January 1 of the year following the enactment of the legislation. The taxable gain was to have been measured in the conventional way—net proceeds of sale or liquidation in excess of one's investment in the corporation.

O Continued

Generally, the impact of this tax could be at a rate of 40% on corporate shareholders or 20% on trusts and individual shareholders. Clearly, such a new tax law could have adverse consequences for a sale of a corporate investment in U.S. property held by a foreign person. A British Virgin Island (BVI) corporation's holding of a U.S. subsidiary with a U.S. condominium could, for example, be one of the investments affected upon a future liquidation of the U.S. corporation.

To combat this proposed tax, the use of partnerships to hold U.S. investments has been strongly reconsidered. Use of partnerships has not been popular in the past mainly due to the fact that, unlike corporations, it is unclear whether partnership interests are considered foreign situs property which would be exempt from the U.S. estate tax.

b. Holding title to real estate – should ownership be held directly for a foreign corporation?

Some advisors favor investment in U.S. real property directly through ownership by a foreign corporation if this can be accomplished through a treaty country that has a **non-discrimination clause in the treaty to prohibit branch profits tax**. The following treaties preclude or contain language which should preclude the imposition of the U.S. branch profits tax on qualified residents of these countries.

Belgium	Greece	Jamaica	Pakistan
China	Hungary	Korea	Philippines
Cyprus	Iceland	Morocco	
Egypt	Italy	Norway	

Foreign corporations from these countries should probably elect to be treated as a domestic U.S. corporation by making the election under IRC Section 897(i) as described in Question G. In these circumstances, the protection from estate tax is the same as the parent-subsidiary structure described in Question O, 1, a above.

Other tax treaties allow for the branch profits tax to be imposed at a lower treaty rate of 4%. These treaties include the following countries:

Australia	Denmark	Ireland	Luxembourg	Russia	Switzerland
Austria	Estonia	Japan	Mexico	Slovakia	Ukraine
Barbados	Finland	Kazakhstan	Netherlands	Slovenia	United Kingdom
Canada	France	Latvia	New Zealand	South Africa	Venezuela
Czech Republic	Germany	Lithuania	Poland	Sweden	

O Continued

Other treaty countries allow for reduced rates anywhere from 10% to 15%.

Current U.S. law allows the sale of the stock of a non-electing foreign corporation holding U.S. real property without requiring the recognition of gain. However, **this sale would contain a hidden tax liability to the buyer** when the real property is ultimately sold since the real property would still have the original cost basis to the corporation. If, on the other hand, an 897(i) election had been made by the corporation, the sale of the stock would be taxable and subject to FIRPTA withholding.

c. Are the costs of carrying an investment in U.S. property by a foreign owner deductible in determining taxable gain when the property is sold?

Such costs as **mortgage interest, real estate taxes**, and **maintenance** costs are **not allowed as deductions** in circumstances described in Question O, 1, c, I below, **but** they are **deductible** in other circumstances described in Question O, 1, c, II below.

i. Such costs are **not allowed** as deductions and are **lost forever** if the property is owned by **foreign individual(s)** and:

- a timely filed U.S. income tax return is not filed (i) to report and deduct mortgage interest and real estate taxes paid on behalf of unimproved and unproductive real property, or (ii) timely filed to claim deductions above for income producing property; or

- the property is unimproved and unproductive real property which produces no income and a timely filed election included with a U.S. income tax return to capitalize mortgage interest and real estate taxes for the y ear was not filed; or

- the property is being developed or improvements are being constructed and a timely filed election included with a U.S. income tax return to capitalize the costs above as well as construction costs for the year was not filed.

For foreign corporations:

- a timely filed U.S. income tax return is not filed to report the deductions described above when connected with a U.S. trade or business; or

- the property is unimproved and unproductive property not involved in a U.S. trade or business; or

- the property is income producing property and not involved in a U.S. trade or business.

ii. Such costs described above may be allowed as deductions if the property is:

- owned by a U.S. corporation; or

- owned by a U.S. partnership; or

- owned by foreign individual(s) or foreign partnership, mortgage interest and real estate taxes are deductible if a timely filed U.S. income tax return is filed when (i) related unimproved and unproductive property, or (ii), timely filed to report all deductions described above for income producing property; or

- owned by a foreign corporation, the expenditures described above are deductible even if not engaged in a U.S. trade or business (i) as long as a timely election is made in the first year income was received by the corporation in order to be "deemed" as conducting a U.S. trade or business, and (ii) to the extent the deductions are connected to U.S. effectively connected income.

The Internal Revenue Service has previously provided some leniency to foreign individuals who have filed late U.S. income tax returns where the preservation of deductions may be achieved by the foreign individual who, in certain instances, can show they acted reasonably and in good faith in failing to file timely. Recent IRS actions and court decisions indicate that the IRS is more aggressively rejecting late filed returns and denying deductions to taxpayers who previously would have met the reasonable cause exemptions. In this climate, it is more critical than ever to timely file tax returns and disclosures.

d. Why should a foreign investor in U.S. real estate file annual U.S. income tax returns when the property produces income, but does not produce enough net income to result in a U.S. income tax liability?

As indicated in the foregoing paragraph, many foreign investors who own U.S. property lose important tax benefits because they fail to **file annual income tax returns** and **make important elections** with the tax returns regarding income producing property.

The failure to file annual tax returns, even when no tax is due, can subject gross rental income to a withholding tax (up to 30% plus penalties) and cause loss of deductions for carrying charges such as mortgage interest and real estate taxes and maintenance costs which would otherwise be useful in reducing U.S. taxes on gains when the property is sold. Fortunately, the withholding requirement does not pertain to the conduct of a U.S. trade of business. Under appropriate circumstances an election can be made for U.S. real property which produces income to treat the property as a U.S. trade or business for tax purposes. This election can only be made on a timely filed income tax return. The foreign investor who can properly make this election to treat the property as a U.S. trade or business or who, in fact, is operating a trade of business, should request the tenant not to withhold taxes from each rent payment. This request should be made by completing Form W-8ECI and providing the tenant with a copy. Form W-8ECI puts the tenant on notice that the rental property is declared to be a U.S. trade or business and that the foreign investor is filing a U.S. income tax return, therefore, no withholding is required.

The tenant is required to withhold and remit to Internal Revenue Service 30% of all gross rent payments to foreign persons, unless this rate is reduced by a treaty, or unless the foreign person has supplied the tenant with **Form W-8ECI.** If the withholding requirement applies, it is required even if the rent is not sent directly to the foreign owner. For example, unless the rent is exempt from withholding, as described above, if the monthly rent payments are collected by a management company and the funds are used to pay real estate taxes and other costs of maintaining the property, withholding is applied to the **gross rents**.

In cases where the 30% tax is withheld, the investor may obtain substantial refunds by filing a U.S. income tax return and declaring his expenses of carrying the property plus depreciation.

In some cases, when no withholding occurred, Internal Revenue Service has deemed the amount received by a foreign person to be **net** of required withholdings. The Internal Revenue Service then took the position that the gross rent paid was only 70% of the actual rent. Internal Revenue Service then **increased** the rental income of the foreign recipient by the amount deemed withheld and assessed the tenant for failure to remit the 30% required withholding. This is not only a concern of the tent. Internal Revenue Service may, upon failure to collect from the tenant, look to the foreign person who owns the property for payment of the tax due.

The foreign investor is required to file U.S. tax returns and report rental income from property without regard to whether the tenant withholds from each payment. Following proper procedures will protect the interests of both tenant and landlord.

In order to file a U.S. income tax return, an individual must either possess a U.S. social security number or a U.S. individual taxpayer identification number (ITIN) if the individual is not eligible to apply for a U.S. social security number. Please reference Appendix B for the procedures to apply for an ITIN.

e. Should U.S. investments be financed by loans or contributions of capital?

CORPORATIONS

Generally (except for qualifying "portfolio interest" discussed in Question E, 1, c) all interest paid to foreign lenders is subject to U.S. withholding taxes at a 30% rate or lower treaty rate. A corporation generally cannot deduct excess interest on a **related** foreign lender's financing if it has a debt-to-equity ratio in excess of 1.5 to 1, unless the interest is subject to the full 30% withholding tax rate. Debt-financed investments work well in some circumstances and are very costly in others. **Each debt structure should be carefully considered by your tax advisor before it is set in place.**

Loans differ from capital contributions in that loans are deemed, under Internal Revenue Service regulations, to bear interest. The interest on loans is subject to withholding but the loan principal repayments are not. Capital is not required to bear interest and is thus not subject to interest withholding. However, the entire amount of repayments of capital (other than liquidating distributions) can be subject to the 30% withholding tax rate or at a reduced treaty rate. **If repayments of capital are contemplated, before the liquidation of the company, careful consideration should be given to funding the company with loans rather than capital contributions**.

A further "trap" to avoid is having an **individual** non-resident alien loan funds to the U.S. corporation. Such loans, absent treaty protection, are included in the taxable estate of the non-resident alien. The value of the shares in the U.S. corporation, if held by a foreign parent corporation, would be excluded from the taxable estate, but the loan held by the individual would not be. Accordingly, the loan should be made by an "unrelated" corporate entity or trust owned by a non-resident alien.

"Unrelated" is important to avoid withholding tax on the interest paid on the loan (See definition of Portfolio Interest discussed in Question E, 1, c).

INDIVIDUALS

See Question F, 4 for important information on how "non-recourse loans" serve to reduce estate tax on individually held properties.

f. Legacy trusts which are referred in Question G, 9 are common in the right circumstances. Ideally these structures for holding real estate or other assets offer the lower individual tax rates and estate tax protection. More information on this structure is available upon request.

2. HOW TO HOLD U.S. BANK ACCOUNTS AND CERTIFICATES OF DEPOSIT

These investments **may be held individually by non-resident aliens or held by foreign corporation since they are not subject to U.S. income taxes or U.S. estate taxes** unless effectively connected with a U.S. trade or business. Form W-8BEN must be filed with the institutions holding these investments in order to declare their non-taxable status. If Form W-8BEN is not filed, the interest on these accounts will be subject to withholding tax. Note: As discussed in Question E, 1, b, the Internal Revenue Service has proposed for financial institutions to annually report U.S. bank deposit interest paid to certain U.S. non-resident individuals.

3. HOW TO HOLD ALL OTHER INVESTMENTS

All other U.S. investments as well as indebtedness of U.S. entities to foreign persons other than certain portfolio obligations described in Question E, 1, c should **generally** be held by a foreign corporation or trust with no U.S. beneficiaries for the same **estate tax** reasons as described above with respect to investments in U.S. real estate.

4. WHERE TO PERFORM SERVICES FOR COMPENSATION

When engaged in providing services for compensation – perform the services outside the U.S., if possible.

5. OPERATING A BUSINESS OUTSIDE THE U.S. – WHAT CONSTITUTES A TRADE OR BUSINESS WITHIN THE U.S.

In general, the nature and extent of the economic activities of a foreign corporation determines whether it is engaged in a trade or business.

Since a corporation can be deemed to be engaged in a trade or business in the U.S. through the activities of its employees or dependent agents who are performing services on behalf of the corporation, the sale of goods to U.S. purchasers by a foreign corporation without the use of an office, dependent agent or employees in the U.S., does not constitute a U.S. trade or business. A foreign corporation selling goods in the U.S. on a regular basis may generally avoid U.S. tax by passing the title to goods outside the U.S.

U.S. dependent or exclusive agents used by a foreign corporation for sales will generally deem the foreign corporation to be engaged in a U.S. trade or business if the agent concludes all significant elements of a transaction. The Internal Revenue Service has ruled that a foreign corporation was engaged in a U.S. trade or business by granting the exclusive right to sell its goods in the U.S. on a commission basis to a U.S. corporation.

If the foreign corporation sells its products to a U.S. distributor, such sales arrangement should not cause the foreign corporation to be engaged in a U.S. business. The U.S. distributor could even be a wholly-owned subsidiary, as long as the transactions are at arm's length. **Caution: If the arrangement resembles an agency relationship, the foreign corporation will be engaged in a U.S. trade or business.**

A foreign corporation which purchases products in the U.S. generally will not, solely because of such activity, be considered engaging in U.S. trade or business. Internal Revenue Service regulations and public policy encourage foreign corporations to come to the U.S. to source their goods. **Caution: Notwithstanding this relatively liberal sounding policy, consideration should be given to establishing a U.S. corporation to conduct purchasing activities for the following reasons: If a U.S. branch of a foreign corporation handles "material" aspects of the transaction, the foreign corporation will be taxed in the U.S.** A foreign corporation sourcing in the U.S. which "crosses over the line" and is deemed to be "materially participating" in the transaction is going to be subject to allocation of its income and expenses. This would have the effect of granting U.S. tax authority over the foreign corporation because the foreign corporation is deemed to have a U.S. office. As a practical matter, this often happens for good business reasons involving the need for closer supervision of the purchasing and shipping activities which leads to more and more material involvement. Generally, purchasing activities alone do not create taxable income beyond the value of the services provided. However, when the U.S. office (or separate corporation) goes beyond pure purchasing functions such as buying and selling as principal or selling on a commission basis, related income is taxable. Transfer pricing rules will apply to all activities entered into for related parties, as discussed elsewhere.

A foreign corporation which sells or licenses technology to a U.S. company and sends its employees to the U.S. to advise and instruct the U.S. company in connection with such sale or licensing, generally will not be considered as engaging in a U.S. trade or business.

Active **real estate** profit-generating activity will be deemed being engaged in a U.S. business. Passive real estate investment does not constitute a U.S. trade or business. Leased U.S. real estate on a regular and continuous basis has been held to be engaging in a U.S. trade or business, including property managed by a property manager (See Question G, 1, a and Question G, 1 b).

The activities of a foreign corporation in the U.S. exploring the business opportunities of entering into a U.S. business, is not engaging in a trade or business.

6. IF YOU ARE INVOLVED IN CROSS-BORDER TRADE, YOU MUST SUBSTANTIATE IMPORT/EXPORT TRANSFER PRICING TO/FROM THE U.S. AMONG "RELATED" PARTIES IN CONFORMITY WITH INTERNAL REVENUE SERVICE REQUIREMENTS

The statutory basis governing transfer pricing is IRC Section 482, which gives Internal Revenue Service authority to allocate income and deductions **among related parties** to "clearly reflect the income" of any such party.

When the same parties **own or "control"** two or more entities, Internal Revenue Service may reallocate gross income and deductions between those entities. **The Tax Court has held that, where parties were acting in concert to advance their own interests, there was "common control" sufficient for the transfer pricing rules to apply.** Generally this applies to advances and loans, sales of tangible property, services, leases, and transfers of intangible property.

The language in the 1994 regulations regarding control among taxpayers acting "with a common goal or purpose" was derived from a line of tax cases. The regulations state that "control" includes any kind of control, direct or indirect, whether legally enforceable or not, and however exercisable or exercised, including control resulting from the actions of **two or more taxpayers acting in concert or with a common goal or purpose.** It is the reality of the control that is decisive, not its form or the mode of its exercise. A presumption of control arises if income or deductions have been arbitrarily shifted. The regulations are deliberately vague. The Court Appeals held in a decision that **"the burden is on the Government to prove the shifting of income if that fact is to create a presumption of common control." Without evidence to support this fact, the presumption of correctness is on the side of the taxpayer.** The arrangements between apparently unrelated parties are involved and must be considered carefully in consideration of the impact of the "common interest" principle on the "common control" requirement under IRC Section 482.

The regulations accept that a transfer price reflects income so long as it falls within an arm's- length range. The defensibility of an adopted transfer price must be established by reference to comparables. So long as a proposed comparable is "sufficiently similar to provide an arm's-length result," the comparable may be considered in determining an arm's-length result. This means comparables do not need to be exact. Successful defense of transfer pricing cases requires much more analysis that "reasonableness tests." Prices need to be set as if the parties were economically independent.

The regulations place the greatest emphasis on the necessity of contemporaneous documentation in order to substantiate the transfer prices adopted. Contemporaneous documentation, which includes the most currently available third-party data to substantiate the pricing adopted and reported for tax purposes, can serve as a demonstration of good faith to avoid potential penalties.

P. WHAT ARE THE INDIVIDUAL AND CORPORATE INCOME TAX RATES IN EACH STATE?

Table P-1 – Individual Rates as of December 31, 2012

Alaska, Florida, South Dakota, Texas, Nevada, Washington and Wyoming have no individual income taxes. Although each of the other states enacts their own tax laws and methods of computing taxes, the following are the highest marginal individual income tax rates. Taxpayers are now entitled to make an election to deduct state and local sales taxes in lieu of income taxes. Generally, this provision benefits residents of states that do not impose state or local income taxes.

STATE	HIGHEST MARGINAL RATE (2)	RATES APPLY TO SINGLE INDIVIDUAL'S TAXABLE INCOME IN EXCESS OF: (3)
Alabama	5.00%	$3,000
Arizona	4.54%	150,000
Arkansas	7.00%	33,200
California	12.30%	680,000
Colorado	4.63%	Of Federal Taxable Income
Connecticut	6.70%	400,000
Delaware	6.75%	60,000
District of Columbia	8.50%	40,000
Georgia	6.00%	7,000
Hawaii	11.00%	200,000
Idaho	7.40%	10,350
Illinois	5.00%	Of Federal AGI
Indiana	3.40%	Of Federal AGI
Iowa	8.98%	66,105
Kansas	4.90%	15,000
Kentucky	6.00%	75,000
Louisiana	6.00%	50,000
Maine	7.95%	29,900
Maryland	5.75%	250,000
Massachusetts	5.25%	Ordinary Income
	5.30%	Interest and Dividends
	12.00%	Capital Gains
Michigan	4.25%	Of Taxable Income
Minnesota	7.85%	117,061
Mississippi	5.00%	10,000
Missouri	6.00%	9,000
Montana	6.90%	16,400
Nebraska	6.84%	40,000
New Hampshire	5.00%	On Dividends & Interest
New Jersey	8.97%	500,000
New Mexico	4.90%	16,000
New York	8.82% (1)	1,000,000
North Carolina	7.75%	80,000
North Dakota	3.99%	388,350
Ohio	5.925%	208,501
Oklahoma	5.50%	8,700
Oregon	9.90%	125,000
Pennsylvania	3.07%	Of Taxable Compensation
Rhode Island	5.99%	129,900
South Carolina	7.00%	14,000
Tennessee	6.00%	On Dividends & Interest
Utah	5.00%	5,500
Vermont	8.95%	388,350
Virginia	5.75%	17,000
West Virginia	6.50%	60,000
Wisconsin	7.75%	232,600

(1) New York City imposes an additional maximum rate of 3.648% tax in addition to the New York State tax. New York State legislation eliminated the New York City non-resident earnings tax effective July 1, 1999. (2) Certain other cities also impose income tax. (3) Amounts below the indicated amounts are subject to lower tax rates or are exempt.

Table P-2 – Corporate Income Tax Rates as of December 31, 2012. Nevada, South Dakota, Washington and Wyoming have no broad-based corporate income taxes. Note: Washington state imposes a “gross proceeds” tax which varies depending on industry. Examples are: .471% for retailing and 1.5% of gross income for service activities.

STATE	MAXIMUM REGULAR CORPORATE INCOME TAX RATE	(1) “S” CORPORATIONS TAXED ON INCOME
Alabama	6.50%	
Alaska	9.40%	
Arizona	6.97%	
Arkansas	6.50%	
California	8.84%	TAXABLE
Colorado	4.63%	
Connecticut	7.50%	
Delaware	8.70%	
District of Columbia	9.98%	TAXABLE
Florida	5.50%	
Georgia	6.00%	
Hawaii	6.40%	
Idaho	7.40%	
Illinois	7.00%	TAXABLE
Indiana	7.50%	
Iowa	12.00%	
Kansas	7.00%	
Kentucky	6.00%	
Louisiana	8.00%	
Maine	8.93%	
Maryland	8.25%	
Massachusetts	8.00% Plus Asset Tax	TAXABLE
Michigan	6.00%	TAXABLE
Minnesota	9.80%	
Mississippi	5.00%	
Missouri	6.25%	
Montana	6.75%	
Nebraska	7.81%	
New Hampshire	8.50%	TAXABLE
New Jersey	9.00%	
New Mexico	7.60%	
New York	7.10% Plus Asset Tax	TAXABLE
North Carolina	6.90%	
North Dakota	5.15%	
Ohio	0.26%	
Oklahoma	6.00%	
Oregon	7.60%	
Pennsylvania	9.99%	
Rhode Island	9.00%	TAXABLE
South Carolina	5.00%	
Tennessee	6.50%	TAXABLE
Texas (2)	1.00%	TAXABLE
Utah	5.00%	
Vermont	8.50%	
Virginia	6.00%	
West Virginia	7.75%	
Wisconsin	7.90%	

Local taxes may also be imposed on corporate income. (1) States may have certain withholding requirements for non-resident shareholders. (2) The State of Texas assesses a corporate business margin tax that is generally calculated by taking 0.5% or 1% (depending on entity type) of taxable margin for the privilege period. Entities with total computed tax of less than $1,000 or annualized business revenue less than or equal to $1,000,000 are exempt from tax, but may be required to filed a No Tax Due Information Report (Form 05-163).

Note: When comparing the tax rates among the various states, it is important to consider “ad valorem” property taxes and sales taxes to determine which states impose the highest taxes in individual circumstances. Also, as with individual income taxes, differing methods of computation and differing bases of assessment from state to state make true comparability very difficult.

Q. WITH WHICH COUNTRIES DOES THE U.S. HAVE INCOME AND/OR ESTATE AND GIFT TAX TREATIES?

1. <u>TREATIES BETWEEN THE U.S. AND FOREIGN COUNTRIES - INCOME, ESTATE & GIFT</u>

   a. Income tax treaties:

Australia	Egypt	Italy	New Zealand	Spain
Austria	Estonia	Jamaica		Sri Lanka
Bangladesh	Finland	Japan	Norway	Sweden
Barbados	France	Kazakhstan	Pakistan	Switzerland
Belgium	Germany	Korea	Philippines	Thailand
Bermuda	Greece	Latvia	Poland	Trinidad & Tobago
Bulgaria	Hungary	Lithuania	Portugal	Tunisia
Canada	Iceland	Luxembourg	Romania	Turkey
China	India	Mexico	Russia	Ukraine
Cyprus	Indonesia	Morocco	Slovak Republic	United Kingdom
Czech Republic	Ireland	Netherlands	Slovenia	Venezuela
Denmark	Israel	Netherlands Antilles	South Africa	

The former U.S./U.S.S.R. income tax treaty applies to the countries of:

Armenia	Georgia	Tajikistan
Azerbaijan	Kyrgyzstan	Turkmenistán
Belarus	Moldova	Uzbekistan

   b. Estate and gift tax treaties:

Australia	France	Italy	Sweden
Austria	Germany	Japan	Switzerland
Denmark	Greece	Netherlands	South Africa
Finland	Ireland	Norway	United Kingdom

The U.S. has gift tax treaties with:

Australia	Denmark	Germany	Sweden
Austria	France	Japan	United Kingdom

All treaties have exchange of information provisions with the U.S. There is no separate estate or gift tax treaty with Canada, but the income tax treaty includes estate and gift tax provisions.

2. TREATY ELECTIONS

Eligible taxpayers can make elections to override certain provisions of the U.S. tax law for preferential U.S. income tax treatment. Some common elections include individuals to be considered U.S. non-residents who otherwise would be considered dual income tax residents (See Question D) and overriding some of the withholding provisions on U.S. source income (See Question G).

a. Treaty "tie-breaker" election

As discussed in Question D, there are times when a non-resident can be considered a U.S. tax resident as well as a resident of their home country. An eligible individual can make an election to be taxed in only one country to avoid potential double taxation if treaty provisions permit.

A "tie-breaking" election is made by filing a form 1040NR (U.S. non-resident tax return) along with Form 8833. Both forms are filed together and are due april 15th following the calendar year for which the election is to be effective (or, if wages were earned by the individual, on June 15th). An individual will not be deprived of making the election if the forms are filed late although a penalty of $100 can be imposed. However, not filing a timely income tax filing can deprive a U.S. non-resident of deductions to reduce U.S. income. For example, a U.S. non-resident who rents U.S. real property but does not file a timely return can be deprived of all costs associated with the rental such as depreciation and property taxes and would be taxed on the gross rental income.

Note that items of income that would otherwise be taxed in the U.S. but are not because of the "tie-breaker" election are reportable treaty positions and must be disclosed on Form 8833 if they exceed $100,000.

b. <u>Reductions or exemptions of U.S. income tax</u>

An income tax treaty may overrule or modify a provision of the U.S. tax law. If such a position is taken, it is usually necessary to be disclosed to the Internal Revenue Service on Form 8833 along with filing an income tax return. If an income tax return is otherwise not required to be filed, Form 8833 should still be filed with a return that includes the taxpayer's name, address, identification number, and a signature under penalties of perjury. Some instances where a treaty position is to be disclosed include:

- Foreign corporation claiming an exemption or reduction of the branch profits tax discussed in Question O, b.
- Reduction or elimination of tax upon disposition of a U.S. real property interest discussed in Appendix A. Note that this is a narrow exception because FIRPTA legislation has largely eliminated potential treaty benefits on the sale of U.S. real property.
- Reduction or elimination of interest paid by branch of foreign corporation (See Question G, 17).
- An eligible individual wishes to claim a reduced rate of withholding or elimination of withholding on fixed and determinable U.S. source income where no Form 1042-S is filed by the U.S. withholding agent.

If a required treaty position return is not filed, a $1,000 penalty per income item may be imposed. Treaty benefits, however, are not denied for failing to timely file Form 8833.

APPENDIX A

REAL ESTATE AND THE FOREIGN INVESTOR – THE MOST COMMONLY ASKED QUESTIONS ABOUT TAX WITHHOLDING REQUIREMENTS UNDER THE FOREIGN INVESTORS REAL PROPERTY TAX ACT (FIRPTA)

1. **To whom do the rules apply?** Since December 31, 1984 any non-U.S. person or entity which **sells** a U.S. real property interest (USRPI) is subject to FIRPTA withholding requirements. The **buyer** is held liable to withhold the funds (See #9 below).

2. **What is a USRPI?** A U.S. real property interest includes not only direct ownership of real property located in the U.S., but also an interest (except as a creditor) in a U.S. corporation, partnership, trust, or other business entity that holds an interest in U.S. real property. Such an interest includes ownership, co-ownership, leasehold interest, option or time-sharing interest or any other direct or indirect right to share in the appreciation in value of U.S. real property.

3. **What sales are exempt from withholding?** Sales of **residential property** $300,000 or under which the buyer intends to use as a "**residence**" are exempt from withholding. A U.S. real property interest is acquired for us as a "**residence**" if on the date of transfer, the buyer has definite plans for himself or any member of his family to reside at the property for at least 50 percent of the number of days that the property is used by any person during each of the first two 12-month periods following the date of transfer. Days of vacancy do not count. All other sales, regardless of amount, are subject to withholding. Thus, the acquired property does not need to be a **principal residence** of the buyer to qualify for the exemption.

   NOTE: There is legislation that may be considered which would propose that this exemption to withholding be repealed due to perceived abuse.

4. **What is the withholding percentage?** 10% of the **gross** selling price is required to be withheld.

5. Is there a withholding requirement when the investment is sold at a loss? Yes, but the amount to be withheld can be reduced or eliminated by obtaining a "certificate of reduced withholding" from Internal Revenue Service.

6. **How is the certificate of reduced withholding obtained?** An application for this certificate must be filed with the Internal Revenue Service.

7. **How long does it take to obtain a certificate of reduced withholding?** In their publications, the Internal Revenue Service states that the department tries to act upon an application for a certificate no later than 90 days after the application is received.

8. **Is a U.S. income tax return required to be filed for the year of the sale?** Yes, a U.S. income tax return is required even if the sale resulted in a loss. State income tax returns may also be required (except for individuals selling property in a state that does not have an individual income tax, such as Florida.)

9. **Who is responsible to withhold funds at the time of sale?** The **buyer** or the **buyer's agent** is responsible to withhold and remit the funds to Internal Revenue Service.

10. **What is done with the amount withheld?** The funds must be remitted to Internal Revenue Service within 20 days of closing unless an application for reduced withholding has been filed with Internal Revenue Service as of the time of closing.

11. **What is required if an application for a certificate of reduced withholding has been filed with Internal Revenue Service, but no determination has been made as of closing?** The required withholding amount is placed in escrow (usually with the buyer's attorney or title company) until the Internal Revenue Service reaches a determination.

12. **Why place the funds in escrow instead of remitting to Internal Revenue Service?** If funds are placed in escrow, funds can be disbursed directly to the seller once a determination letter is received. It can take months to obtain a refund from the Service even after obtaining a determination letter (See #17 below).

13. **Who may request a certificate of reduced withholding?** Either the buyer or seller may request a certificate of reduced withholding, but usually the seller makes the request. (A CPA usually prepares the application.)

14. **What documents are needed to apply for a certificate of reduced withholding?** In general, the documents needed are documents sufficient to establish cost basis, the amount of gain or loss, and that there is no unsatisfied FIRPTA withholding tax requirement. Examples of such documents are: contract for ale, closing statements for original purchase of property, invoices and canceled checks to document improvements made to the property, copies of income tax returns where applicable, name, address and federal identification number of buyer, certificate of reduced withholding, or certificate of non-foreign status obtained of original purchase of property if purchased after December 31, 1984, and such other documentation as may be relevant to a specific property. These examples are not the only documentation which would be acceptable, nor is every item required in every filing.

    Also of great importance is the requirement, as of November 3, 2003, to provide U.S. taxpayer identification numbers of both the purchasers and sellers to the transaction. Refer to #21 for additional documentation required if either the foreign transferor or transferee do not have either a U.S. social security number of U.S. individual taxpayer identification number (ITIN).

15. **When must the request for the certificate of reduced withholding be filed?** The request for the certificate can be filed either before or after the sale, but before the due date of the seller's income tax return for the year of sale.

16. **What if the request for the certificate of reduced withholding is not filed in time?** The full 10% of the gross sales price is submitted to the Internal Revenue Service by the withholding agent as a function of law.

17. **How can I get a refund if the 10% remitted to the Internal Revenue Service is more than my actual tax liability?** A refund can be obtained by the taxpayer by having a tax professional complete an "early refund" application or by waiting to file the required U.S. income tax return.

    The "early refund" serves to accelerate the time it would take to receive a refund if the disposition of property takes place many months before tax filing is required. This "early refund" procedure can also be used where a withholding certificate had been applied for and granted but with an incorrect withholding amount. There is no particular form for this refund application but there is specific information the Internal Revenue Service requests to be submitted using a special numbering system. The information to be submitted is substantially similar to the application for a reduced withholding certificate discussed above with the exception of an Internal Revenue Service stamped Form 8288-A to be included as an attachment. This procedure does not eliminate the requirement to file a subsequent U.S. income tax return to report the sale of U.S. property.

    Alternatively, a refund can be requested on the seller's income tax return for the year of the sale. The income tax return is normally filed by June 15 of the year following the sale in the case of non-resident aliens; by April 15 in the case of estates, trusts, and partnerships; and by March 15 of the year following the sale in the case of corporations. These dates are filing deadlines (excluding extensions) imposed by the Internal Revenue Service. It is common for these returns to be filed earlier than the filing deadlines in situations where a refund is expected. Taxpayers can file tax returns as soon as they are released by the Internal Revenue Service in final form. In some cases, such as corporate taxpayers, the release of tax forms may occur as early as January.

    A refund may generally be requested on the income tax return for the year of sale, even if filed late. However, **a refund will not be issued for an original return filed more than two years after the tax was paid.** The Internal Revenue Service applies specific rules to tax withheld at source with respect to income of non-resident individuals and non-resident corporations to determine when tax is required to be paid. The Internal Revenue Service deems these taxpayers to have paid tax on the last day prescribed for filing (without regard to any extension or exemption from filing) the return for the year in which the tax is allowable as a credit. For example, taxes withheld in connection with a property sale taking place July 8, 2004 and remitted to Internal Revenue Service on July 27, 2004 will not be refunded on an original return filed after June 15, 2007 assuming a non-resident individual sold the property. The original due date for U.S. non-resident filers who do not earn wages is June 15th of a calendar year. If an income tax return had been filed for 2006, but did not include a request for refund of FIRPTA taxes over withheld, a refund may be requested on an amended return filed within three years of the date the return for 2006 was filed.

18. **How long does it take to receive a refund?** A refund requested on the income tax return of the seller will usually take 6-8 weeks from the time it is filed. An early refund requested under the FIRPTA administrative rule usually takes longer from the time of request, but the request may be filed before the end of the calendar year of the sale.

19. **What if the property is sold under an installment agreement?** In general, the transferee is required to withhold on the full sales price regardless of the amount of the payment. However, if the transferor is not a dealer and will report gain using the installment method, permission may be obtained to report and remit payments under the installment method. An application for permission to use the installment method to remit payments will be based on the transferree's agreement to:

    a. Withhold and pay over 10% (or the lower amount determined by Internal Revenue Service to be appropriate) of the down payment including any liabilities of the transferor assumed by the transferee.

    b. Withhold and pay over 10% (or the lower amount determined by Internal Revenue Service to be appropriate) of each subsequent payment plus interest on the deferred tax liability.

    c. Pay over all amounts withheld from the transferor's proceeds and include transferor's identification number.

    d. Notify the Internal Revenue Service before the disposition or encumbrance of the U.S. real interest and, when it occurs, pay over the remaining amount to be withheld.

    e. Continue to withhold under a reduced withholding certificate until an amended certificate is issued.

20. **What disclosure of the seller and buyer's identities are required?** With regulations instituted in 2003, the Internal Revenue Service requires all parties (purchaser and seller) to have either a U.S. social security number or a U.S. individual tax payer identification number (ITIN) listed on any application for reduced withholding that a foreign seller wishes to apply for. The regulations effectively accelerate the time by which the foreign person would be required to obtain an identification number. The process to obtain this number has also been changed substantially (Refer to Appendix B). When applying for a U.S. ITIN< the foreign individual utilizes Form W-7. This form requires the foreign individual to provide their full name, mailing address as well as foreign home country address, date of birth, country and province of birth, country of citizenship, foreign taxpayer identification number (if any), and U.S. visa information (if any). Documentation (such as foreign country passport or foreign birth certificates) is also required to be submitted with Form W-7 when applying for an ITIN. Please reference Appendix B for more information.

21. How do regulations issued August 4, 2003 affect applications for reduced withholding certificates and real estate closings in general? What is new is the requirement for ITINs (Individual Taxpayer Identification Numbers) for both buyer and seller as a precondition to approving an application for reduced withholding tax as well as the remittance of the 10% withholding tax to the Internal Revenue Service even if an application for reduced withholding does not take place. The requirement for having these ITINs is new and so is the process in obtaining them. Obtaining an ITIN is no longer automatic and requires considerable more effort and attention by real estate professionals to ensure a smooth real estate closing.

When filing an application for reduced withholding, Firm W-7 must now be submitted with the entire application attached if a foreign transferor does not have a U.S. social security number or an ITIN. Both the Form W-7 and application for reduced withholding are mailed at the address listed in the Form W-7 instructions. Extreme care should be taken when completing form W-7. If this form is not filed to Internal Revenue Service standards, the application for reduced withholding is suspended and not processed until the problem(s) identified by the Internal Revenue Service with Form W-7 is (are) corrected. The application for reduced withholding will be completely rejected if an ITIN cannot be processed, thereby requiring the 10% withholding tax to be remitted to the Internal Revenue Service.

Currently, attention has not been paid to the foreign transferee who lacks an ITIN in this situation. Presumably, Form W-7 is filed on behalf of this individual and Form 8288-B is attached for processing. This issue will most likely be formally addressed as the Internal Revenue Service continues to iron out wrinkles with the new procedures.

If the closing does not involve an application for reduced withholding, the 10% withholding tax must still be timely remitted to the Internal Revenue Service as discussed in #10 above. If either the transferor or transferee does not have a U.S. social security number or ITIN, then Form 8288 and 8288-A must be attached with Form W-7 and supporting documentation in order to obtain an identification number. The package is to be mailed to the address listed in instructions to Form W-7. The Internal Revenue Service will then date stamp Form 8288-A and send to the foreign transferor in order to claim the withholding on the required U.S. non-resident filing to document the sale.

A stamped Form 8288-A will not be mailed to the foreign transferor if form W-7 is not submitted with Form 8288 and 8288-A or if identified problems with Form W-7 are not corrected. A stamped 8288-A is required to be attached to the U.S. non-resident return of the foreign transferor in order to report and claim credit for the 10% when calculating the actual U.S. tax liability. If no ITIN is assigned when required, the foreign person claiming a credit for the FIRPTA withholding must submit Form W-7 along with their form 1040NR, and the settlement statement from the property sale depicting the 10% withholding.

When a transferor exchanges a U.S. real property interest and such exchange qualifies for **non-recognition treatment** under the Internal Revenue Code, the transferor must submit a notice of non-recognition to the Internal Revenue Service. This notice includes the transferor's U.S. identification number, name and address. If the transferor does not have a U.S. social security number or ITIN, then Form W-7 must accompany the notice of non-recognition which is submitted in draft form. Once the identification number is issued, a finalized non-recognition notice is then submitted to the transferee. Failing to provide a finalized non-recognition notice would require that the transferee withhold and remit the FIRPTA tax and file Form 8288 and Form 8288-A.

An example of a non-recognition transaction where a notice is required would be where a foreign individual transfers real property as a contribution of capital to a U.S. corporation they substantially own (e.g., §351 transaction). Additionally, although technically a non-recognition transaction, non-recognition notices cannot be used in a deferred like-kind exchange effective as of September 4, 2003. To avoid having the FIRPTA withholding remitted directly to the Internal Revenue Service in a deferred like-kind exchange, an application for reduced withholding certificate must be applied for prior to closing. Additionally, to avoid partial recognition of tax on the deferred like-kind exchange, the taxpayer must contribute an amount equal to the FIRPTA withholding (10% of the contract price) to the Qualified Intermediary used in the like-kind exchange. This contribution is necessary because the buyer's representative will withhold 10% of the contract price and keep in a separate escrow account while waiting for the Internal Revenue Service to make a final determination on the reduced withholding certificate application. Once a final determination is issued, the funds would be free to be released to the taxpayer to effectively serve as reimbursement for the contribution the taxpayer had to make to the Qualified Intermediary. The Qualified Intermediary would use the sales proceeds as well as contribution by the taxpayer to purchase the replacement property.

APPENDIX B

APPLICATION FOR INDIVIDUAL TAXPAYER IDENTIFICATION NUMBERS (ITIN) UNDER RULES EFFECTIVE AS OF JANUARY 1, 2013.

Please refer to IRS Rev. Proc. FS-2012-11, November 2012
http://www.irs.gov/uac/Newsroom/Updated-ITIN-Procedure-Changes-Announced

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