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Individual Taxation in the US

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Introduction

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Introduction

A changed environment

- US has always been suspicious of US citizens with foreign interests (i.e. extensive reporting requirements)

  But now:

  - Large budget deficits
  - Public intolerance of perceived tax evasion or avoidance
  - Governments want to be seen to be tough
- In the US context, IRS now much more focused on compliance
- Exemplified by Foreign Accounts Tax Compliance Act (FATCA):
  - New Reporting requirements for individual taxpayers
  - Reporting obligations on financial institutions who invest in the US to disclose US investors
  - Going International with reciprocal intergovernmental agreements

RESULT:

- Global information sharing to be the norm
- More US taxpayers becoming compliant and/or giving up citizenship

Who is a US tax resident ?

A US tax resident is subject to US Federal tax on worldwide income

- A US tax resident is:
  - US citizen
  - US Greencard Holder (lawful permanent resident)
  - Someone substantially present in the US (3 year test; > 30 days in the current year plus 183 days in total over the past 3, total year 1 1/3 2nd year 1/6 3rd year)

Who is a US Citizen?

- Someone born in the US
- Someone born to two US citizen parents

- A child of one US citizen, if born outside of the US:
  - If born after 14/11/86, so long as the US parent lived in the US 5 years (2 after age 14)
  - If born before 15/11/86, so long as the US parent lived in the US 10 years (5 after age 14)

2013 US Tax Rates

- Top rate of income tax in 2013 increased to 39.6% (but note Net Investment Income tax and also possible State Taxes)
- Graduated tax bands, level of income determines rate of tax
- Allowances for children and preferential rates for married couples
- Long term capital gains and qualified dividends previously always taxed at 15%, from 2013 for higher earners this is now 20% (example individual with income >$400,000)
- Deductions can be itemized and personal exemptions claimed but from 2013 where an individual has income in excess $250,000 itemized deductions and personal exemptions become phased out.

Net Investment Income Tax (NII)
- New additional tax from 2013

- Applies only to residents
- Form 8960 introduced to calculate 3.8% of net investment income tax
- Introduced to help support “Obamacare” as part of the Affordable Care Act and the Health Care and Education Reconciliation Act
- Tax on certain income and gains that exceed threshold amounts
- NII taxable upon following Income and gains:
  - Interest
  - Dividends
  - Rents, royalties and trading financial instruments
  - Gains on passive income – stocks, bonds, mutal funds, sale of interests in partnerships if passive owner
- Threshold amounts:

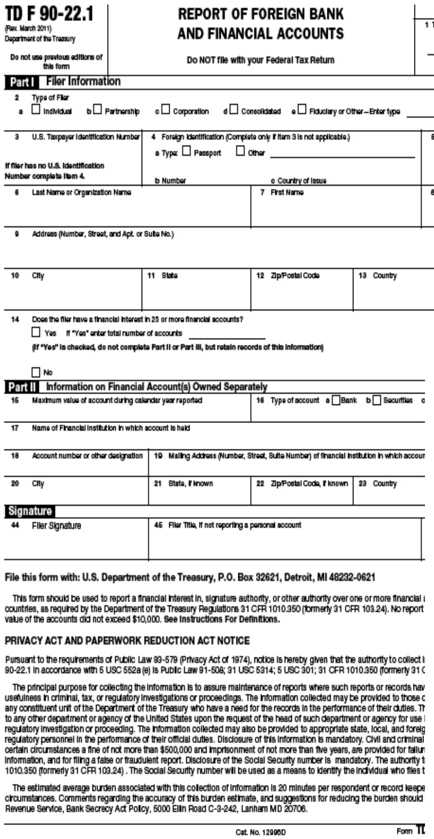
Filing status	Threshold amount
Married filing jointly	$250,000
Married filing separately	$125,000
Single	$200,000
Head of household (with qualifying person)	$200,000
Qualifying widow(er) with dependent child	$250,000

- Individuals taxed upon the lower of their NII or the amount their income exceeds threshold amounts

Estate and gift tax

- Governed by an individual's 'Domicile'
- For resident alien's this is based on an intention to make the US their permanent home
  (a number of factors will be taken into consideration)
- If an individual holds a US Greencard, there will be a presumption of US domicile
- Not all transfers will give rise to a US tax charge – exclusions are as follows:
  - Gifts to charities
  - Gifts of intangible US property if made by non- domiciliary
  - All transfers to a US spouse (if not a US citizen this is capped at $143,000 p.a.)
  - Annual transfers to any individuals up to $14,000 p.a.
  - Lifetime unified gift and estate tax exclusion for 2013 $5,250,000 (for non US citizens this is $60,000 on death)
  - Tax Rates – maximum is 40% on transfers which exceed the exclusion amount by $500,000
  - There is no Russia/US estate tax treaty
  - Note: US has an additional 'Generation Skipping Tax'
  - Non-Domiciliaries often have significant exposure if they own US Real Estate

Foreign Bank Account Reporting ("FBAR")


TD F 90-22.1
(Rev. March 2011)
Department of the Treasury
Do not use previous editions of this form

REPORT OF FOREIGN BANK AND FINANCIAL ACCOUNTS

Do NOT file with your Federal Tax Return

OMB No. 1545-2038

1 This Report is for Calendar Year Ended 12/31

Amended

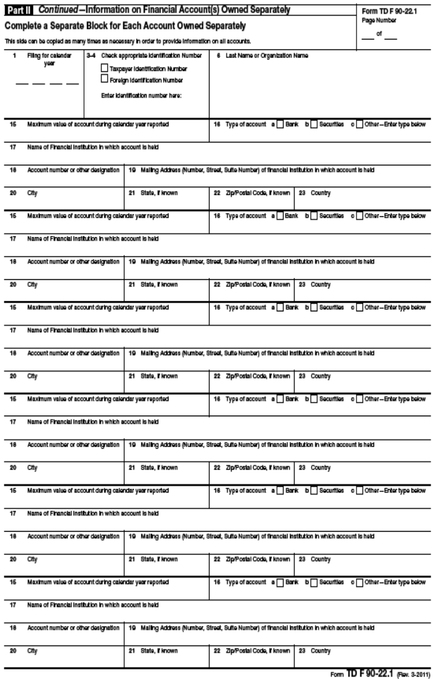
Part I Filer Information

Part II Information on Financial Account(s) Owned Separately

Signature

File this form with: U.S. Department of the Treasury, P.O. Box 32621, Detroit, MI 48232-0621

PRIVACY ACT AND PAPERWORK REDUCTION ACT NOTICE


Part II Continued—Information on Financial Account(s) Owned Separately

Complete a Separate Block for Each Account Owned Separately

Form TD F 90-22.1 (Rev. 3-2011)

- US persons are required to file FBARs annually if they have a financial interest in or signature of other authority over foreign financial accounts
- Aggregate value must exceed $10,000
- Must be received by 30 June
- No extensions granted and failure to file can result in significant criminal and civil penalties
- Civil penalty for wilful failure to file can be as high as greater of $100k or 50% of total balance per violation. Non-wilful violation not due to reasonable cause is $10k
- Substantial revisions and updates to guidance over past few years
- From June 30 2013 must be filed online

Foreign financial asset reporting (Form 8938)

- FATCA imposes new reporting requirements for foreign financial assets owned by US residents (these are ***in addition to*** FBAR reporting requirements)
- Applies where aggregate value of “specified foreign financial assets” exceeds $50,000 during the year
- Form 8938 issued, applied from 2011, various $ reporting threshold

Specified foreign financial asset

- Depository, custodial or other financial accounts maintained by a foreign financial institution
- Stocks and securities issued by a person other than a US person
- Foreign Pensions
- Any financial instrument or contract held for investment with an issuer or counterparty other than a US person
- Foreign Partnership Interests
- Any interest in a foreign entity that is not held in an account maintained by a foreign financial institution

Individual Taxpayer Reporting Thresholds

Filing Status	Value on the last day of the tax year is at least:	Or, at any time during the tax year, is greater than:
Unmarried Taxpayers living in the US	$50,000	$75,000
Married Taxpayers filing jointly living in the US	$100,000	$150,000
Married Taxpayers filing separately living in the US	$50,000	$75,000
Taxpayers not filing a joint return living abroad that are bona fide residents of a foreign country or that are present in foreign countries for 330 full days during a 12-month period	$200,000	$300,000
Married Taxpayers filing jointly living abroad that are bona fide residents of a foreign country or that are present in foreign countries for 330 full days during a 12-month period	$400,000	$600,000

Non-US nationals acquiring US real estate

Direct Ownership	**Advantages** • Preferential capital gains rate **Problems** • Estate and Gift tax exposure • Rental Income
Foreign Corporation	**Advantages** • Minimises US Estate and Gift Tax risk if foreign corporation respected **Problems** • Corporate income tax • Possible deemed rental income where there is personal use • Branch Profits Tax • No capital gains rate • Additional administration costs
Trust	**Advantages** • Can be best of both worlds • Preferential capitals gain rate • Can minimise US Estate and Gift tax risk if properly structured **Problems** • Complexity and additional costs • Potential issues if settlor later becomes US resident and then terminates US residency • Estate tax risk greater if person desiring US residence is also source of funds. • Potentially ineffective if property already owned outside of trust

Offshore Voluntary Disclosure Programme (OVDP)

Initiative for non compliant taxpayers who failed to report taxable income from undisclosed foreign accounts, foreign assets and foreign entities. Previous programs time limited whilst current program open ended.

Two versions:

Streamlined - For individuals with minimal de-minimus tax amounts (<$1,500) due who need to "catch up" for previous three years. (Unlikely to apply)

Main programme - Designed for serious errors and for individuals who are non compliant and who will owe amounts above the de-minimus threshold (requires up to 8 years of returns to be filed)

Advantages:

- Certainty
- No criminal penalties
- No late filing penalties for items such as FBARs and Trust returns

Disadvantages:

- No "middle ground"; one version or the other (but what about honest mistakes?)
- 27.5% surcharge on all foreign holdings related to the non-compliance Still pay interest and late payment penalties on tax underpaid

If honest errors could consider "quiet" disclosure but need to take advice on risks

Complexities for US Citizens living overseas

- Complex tax and reporting rules in respect to “Trust” interests (Foundations generally treated by US as ‘Trusts’)
- Controlled Foreign Corporation (CFC) rules- Complex anti avoidance rules apply where Foreign Corporation controlled by US person
- Controlled Foreign Partnership rules- Complex reporting rules apply where Foreign Partnership controlled by US person
- Passive Foreign Investment Company -Complex anti avoidance rules apply where Foreign Corporation is predominately used to make investments
- Foreign Tax Credit (FTC) calculation

US/Russia Double Tax Treaty
Signed in 1993

- US/Russia DTT attempts to avoid double taxation for individuals who are within the remit of taxation in both jurisdictions by assigning taxing rights. An individual must be a resident of either Russia and/or US to obtain benefits
- US/Russia DTT includes Protocol containing additional clarifications
- DTT has a “Savings Clause”:
  - Applies to current US citizens
  - Allows the US to tax current citizens as if treaty did not exist (a few limited exceptions - unlike some more recent treaties pension growth is not excluded from taxation)
  - Doesn’t apply to Long Term Residents but a treaty claim is deemed to be an expatriating event
- Exchange of information provision
- Russian currency control rules are still applicable
- Double taxation elimination procedure in Russia

Further planning

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