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2018 essential tax and wealth planning guide

Part 3

Get started

Welcome

Dear Reader,

As 2018 has unfolded, the uncertainty surrounding the 2017 US tax law changes has given way to some amount of clarity. Regulatory guidance has been and continues to be issued. Taxpayers have started to model potential impacts of new tax provisions. Reduced income tax rates are welcomed by many, yet other changes have created concerns.

That's just in the United States. What about developments elsewhere around the world? This third edition of Deloitte Tax LLP's *2018 essential tax and wealth planning guide* offers chapters on unique investments and global investing, as well as a bonus feature on cryptocurrencies and an update to the ever-changing tax policy landscape:

- Our section on **Unique investments** describes developments in the art world and the income tax considerations for investing in yachts, airplanes, and other unique investments.
- In the **Globalization** section, we provide insights into recent investment flows across borders, offer tax considerations for establishing or expanding an international portfolio of investments, and discuss cross-border income tax and estate and gift tax issues that you may face.
- **Cryptocurrencies** are increasingly an asset class of their own, so our bonus feature focuses on potential income tax and estate and gift tax implications of these virtual currencies.

As we near the end of calendar year 2018, it's important to identify potential challenges and opportunities that could arise from the continually changing US and global tax legislative environment. Your ongoing awareness of and preparation for the next developments—whatever they are and wherever they materialize—can have profound consequences. By breaking down complex topics and providing practical planning tools and new perspectives, this edition of the *2018 essential tax and wealth planning guide* will continue to be a valuable addition to your reading list in the coming weeks and months as you look again at the aspects of your world that are important to you—your family, your business, and your personal goals.

To find a member of the Deloitte Private Wealth practice who specializes in your area of interest, please contact us at PrivateWealth@deloitte.com.

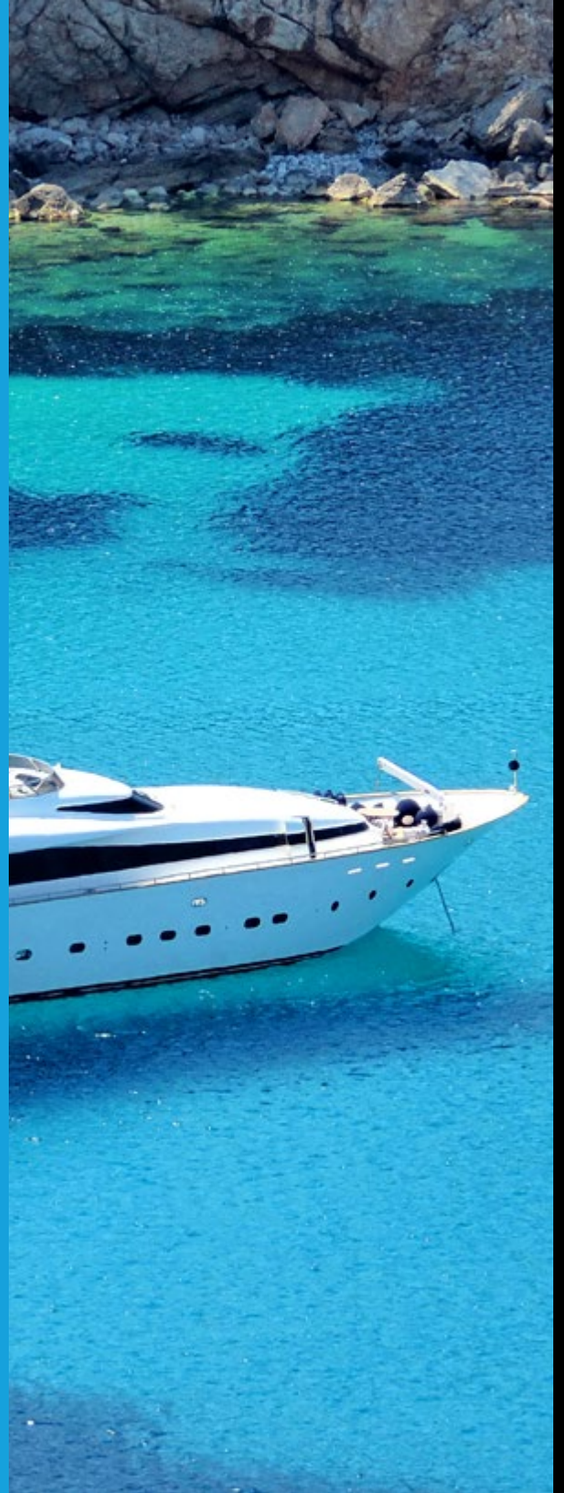
Regards,

Julia Cloud
National Industry Leader
Private Wealth, Deloitte Tax LLP

Contents

Unique investments

Individuals, family offices, and asset managers are increasingly interested in diversification tools for investment portfolios. Examples of these may include art, airplanes, and yachts. Each of these unique investment classes presents specific tax issues in addition to practical and personal considerations.



Art

For individuals and families who maintain an art collection as a substantial portion of their wealth, gift and estate tax planning can be particularly important.

Gift and estate tax planning

Whether you are contemplating lifetime gifts or bequests upon death, the illiquid and hard-to-value nature of artwork makes it a special asset for planning purposes. Such transfers may occur in specialized situations, from simple transfers to heirs to more complex transactions, including partnerships, dynasty trusts, and split-interest trusts. If the decedent transfers these assets to family members upon death, the estate plan should consider how the taxes attributable to the art collection will be paid, given the illiquid nature of the assets.

Philanthropy and charitable planning

Individual donors may be eligible for significant income, estate, and gift tax deductions for charitable donations of art to cultural institutions. It is important to analyze and understand the impact of various donation planning considerations, consult on related-use requirements, and review appraisal requirements for income and transfer tax returns. Additional considerations for charitably inclined taxpayers may include more complex gifts, such as fractional donations and charitable remainder trusts. For art and other tangible personal property with a long-term holding period, the charitable deduction is the asset's fair market value only if the property will be put to a use related to the exempt purpose of the donee charity. If the art is not used by the charity in its exempt function (i.e., related use) for three years after donation, then the donor must recognize income equal to the difference between the fair market value deduction taken and the basis of the property at the time of donation. This recapture can be avoided if the donor obtains a letter from the charity stating that the property was in fact used in its exempt function and how it was used, or certifies that such use has become impossible or infeasible. There is a penalty of $10,000 imposed on charities that inappropriately and fraudulently certify property as being "related-use property."

Art

Fractional gifts of art

Taxpayers should also be aware of the tax issues related to fractional gifts of art. Prior to the Tax Reform Act of 1969, it was possible to donate artwork to a museum, retain the life estate, and receive an immediate income tax deduction. Congress was concerned that art donors were benefiting from the increase in value as the art was on display in a museum setting. As the value increased, donors would donate additional, more valuable fractions with the hope that the value of the deduction would increase over time. The Pension Protection Act of 2006 established two restrictions as follows:

- **Time limitation:** Art must be completely donated by the earlier of 10 years or the death of the donor, or else the income tax deduction will be recaptured and a 10 percent penalty tax will be imposed.
- **Value limitation:** The value of subsequent fractional gifts is based on the value on the date of the first fractional donation (only subsequent depreciation, not appreciation, is considered).

Fractional donations of art are still an attractive charitable planning alternative, allowing one to spread a gift over a number of years to reduce the limitations on the charitable deduction allowed. However, taxpayers should be aware that there is no longer an enhanced income tax deduction for subsequent donations.

Valuation considerations

If an executor is tasked with selling a collection through a private sale or public auction, then the executor must plan for the income and transfer tax implications. In any estate planning or gift planning situation, valuation will be an important consideration, as will auxiliary costs of insurance, storage, and shipping. Rarely will clients leave a bequest to sell their art and distribute the proceeds to their children, but when they do, an executor's biggest concern may be getting the art into the right auction and at the right auction house to enhance proceeds. The Internal Revenue Service (IRS) is likely to accept the selling price as the value for the estate tax return, and the selling costs will be allowed as an estate tax deduction. When clients leave their art to heirs, valuation is likely to be a major issue between the IRS and the executor. The IRS can also challenge deductions for insurance, storage, and shipping, if it appears the expenses were for the convenience of the heirs, rather than falling clearly within estate administration costs.

The IRS has an established Art Advisory Panel, which includes up to 25 renowned art experts. If a taxpayer's individual, gift, or estate tax return is audited and the value of the art reported on the return exceeds $50,000, the IRS will refer the case to its Art Appraisal Services Group. This group will then leverage the Art Advisory Panel to review and assess the valuation used to determine the value reported on the return. Alternatively, taxpayers can proactively request that the IRS review the appraisal prior to filing an income, gift, or estate tax return. Following the review, the IRS will issue a statement of value and the taxpayer can report the agreed-upon value on the return to avoid possible penalties.

Art

If the art is expensive, or the estate is that of the actual artist, the estate should retain the foremost valuation expert on the particular artist. There is a strong likelihood that the IRS will review the values claimed for the art on the income, gift, or estate tax return, and the IRS may challenge the values reported if the taxpayer does not obtain a statement of value.

Import and export considerations

In some instances, obtaining artwork, collector's pieces, antiques, or cultural property may involve exporting the item from one country and importing it into another. In such cases, it is important to consider both the departure and arrival countries' export and import laws and restrictions prior to acquiring and transporting the item across borders.

For example, certain types of art, artifacts, and antiquities may be restricted or prohibited from export and/or import based on cultural property laws, international agreements, restrictions on materials, formalities on documentation, and other complexities. The assessment of customs duties depends on the proper tariff classification of the item, as determined by factors such as the detailed characteristics of the item and its age, the circumstances of how it was made, and whether the item is a functional object or a collectible as defined by the customs authorities. In some cases, items may be eligible for duty-free treatment. Finally, the proper valuation of the item for export and import purposes must be considered.

The investor must analyze these issues and effectively navigate the complex, global import and export regulations that govern the cross-border movement of artwork, collector's pieces, antiques, and cultural property to identify possible duty reduction planning considerations.

Art

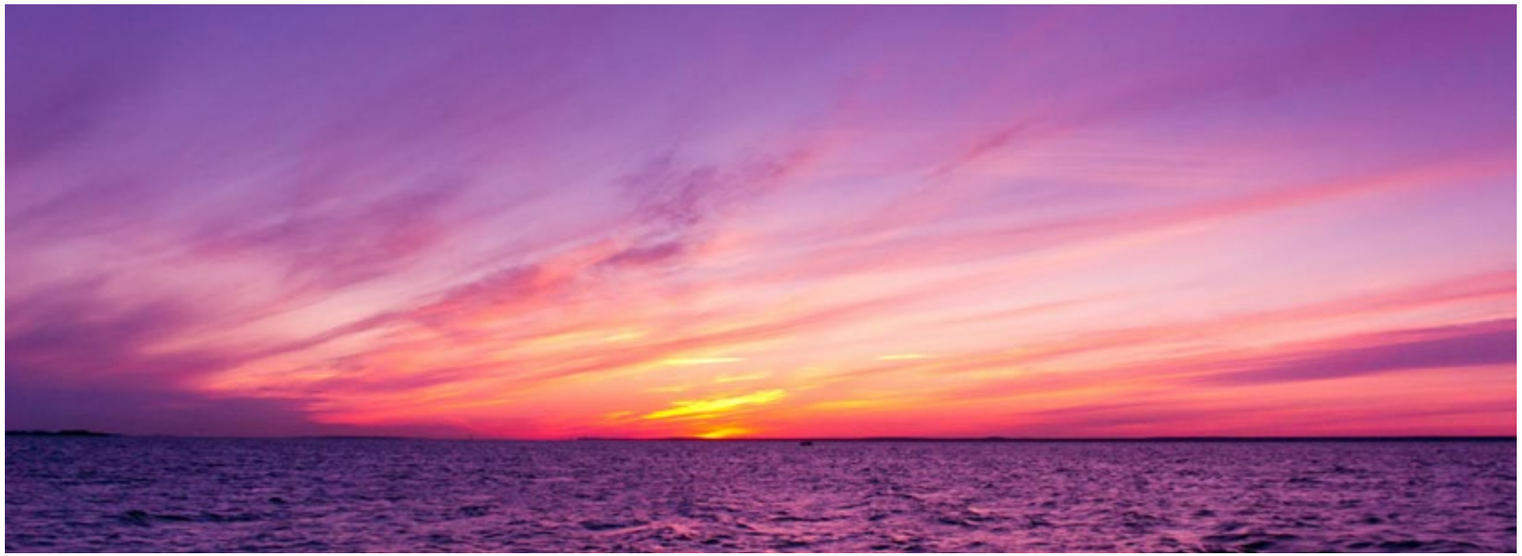
Value-added tax (VAT) and goods and services tax (GST)

There are potential VAT/GST consequences to consider when art is sold, purchased, leased, donated, or simply moved across borders in today's increasingly globalized economy. More than 150 countries in the world have some kind of VAT/GST system. With VAT/GST rates ranging up to 27 percent, it is important to fully understand the applicable rules in order to take steps to manage VAT/GST to limit significant additional costs. In the art world, in particular, there are often special tax regimes and complex VAT rules that can apply where goods are sold by auction or donated/loaned to institutions, making it even more important to plan in advance and take steps to correctly understand the position. Consideration should be given to navigating the complex VAT/GST world to mitigate the risk of unnecessary VAT costs to the investor personally or to a business.

US sales and use tax

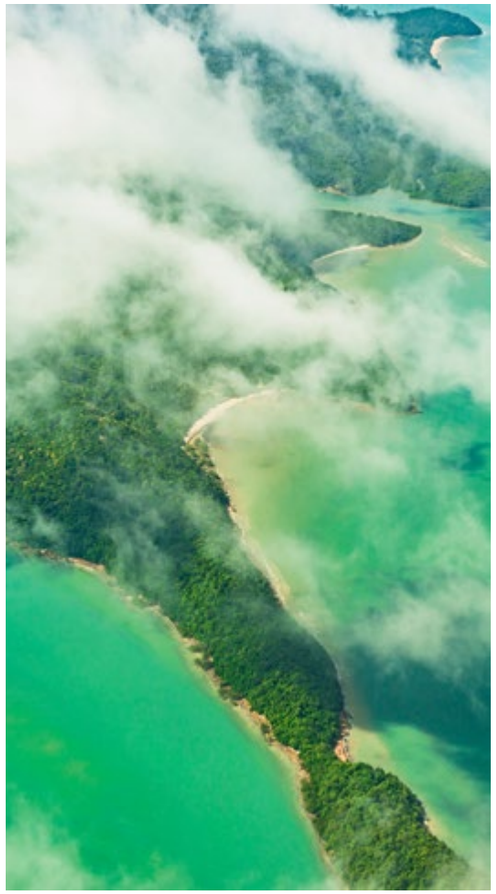
In the United States, 45 states and the District of Columbia impose some sort of sales or use tax with differing exemptions and procedures. As a result, owners, dealers, and collectors will need to consider the potential sales or use tax consequences on purchases and/or delivery within the United States.

Tax planning, tax compliance, and tax controversy services related to purchases or interstate movement of artwork and other collectibles are all important considerations. Each state—and with certain cities within those states—having unique tax laws and factors such as origin, status of seller, initial delivery locations, storage, and final destination of the artwork may impact the tax planning and compliance process. It is important to identify potential issues and tax considerations up front and before the transactions have occurred, so sales and use taxes do not become an unwanted additional expense or surprise.



Airplanes

If you've made the choice to fly private, then addressing the related financial and regulatory compliance requirements is a critical step.



Ownership structure

Understanding the tax implications of flying private can help you choose the ownership structure to appropriately address your specific needs and circumstances. The immediate instinct of most aircraft buyers is to put the plane in a separate legal entity, instead of placing it directly in an operating business, in order to protect the owners from legal liability. Unfortunately, this can create significant tax considerations. From a tax perspective, typically the entity owning the aircraft does not have a trade or business to allow for a full deduction of the aircraft expenses by the owner. Careful planning should be considered to identify the expenses of the aircraft entity that can be used to offset trade or business income of the business it supports. In addition, there are various elections and "grouping" rules to consider.

Payments between related entities can attract federal excise taxes, which are imposed on "air transportation." They also may create a captive flight department company, which may subject them to certain Federal Aviation Administration rules applicable to operators that "carry passengers for hire." Individuals and families should consult competent legal counsel and tax professionals when structuring the ownership of an aircraft.

Under the 2017 Tax Act,[1] aircraft are considered eligible property to qualify for the new 100 percent expensing rules (also referred to as 100 percent bonus depreciation). However, the taxpayer needs to have enough qualified business use of the aircraft in the year of purchase, as well as subsequent years, in order to qualify for the accelerated tax depreciation over the otherwise allowable straight-line method. Additionally, even if there is enough qualified business use to permit the taxpayer to use the 100 percent bonus method, taxpayers should consider examining and limiting personal entertainment usage in the year bonus depreciation is taken to avoid a disallowance of the depreciation expense, along with other fixed and variable expenses of operating the aircraft.

1 An Act to provide for reconciliation pursuant to titles II and V of the concurrent resolution on the budget for fiscal year 2018.

Airplanes

Sales and use tax on aircraft purchases

Many states provide exemptions from sales and use tax for the purchase of an aircraft, such as an exemption for aircraft used in interstate commerce and an exemption for leased aircraft (although the future lease payments may be subject to sales and use tax). In addition, there are flyaway exemptions in various states for the sales tax if the aircraft is not used there; however, there could be a use tax in a different state based upon the aircraft's usage.

It is important to understand if one of the above sales tax exceptions is met in the initial year of purchase and continues to be met for the period of the aircraft's use. The determining factor in concluding which state's taxability rules to apply is the principal hanger location for the aircraft and/or where the aircraft will be located. Individuals who are considering the acquisition of private aircraft should assess whether any sales and use tax exemptions apply prior to taking possession of the aircraft so that the proper paperwork is executed in a timely manner.

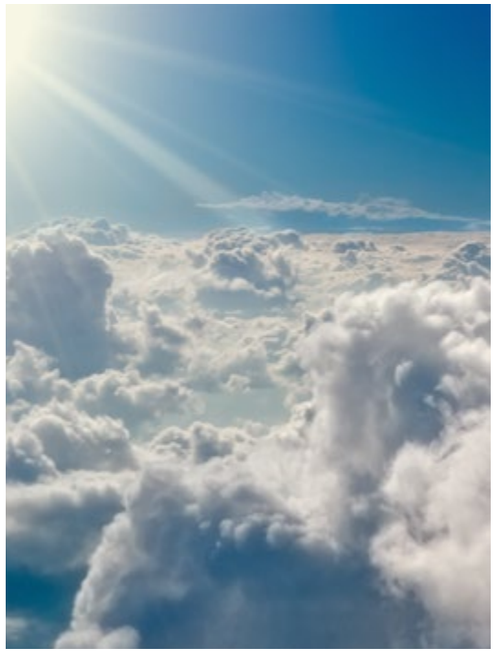
Deductible business expenses

One of the most important questions that must be addressed is when the cost of private aviation is considered an ordinary and necessary business expense.

If business is typically conducted locally or business travel is between major cities that are regularly served by the major airlines, it may be difficult to justify the cost of private air travel as an ordinary and necessary expense of the business. A better argument exists when the business requires flights to out-of-the-way locations without ready commercial air service, the timing and duration of business flights is unpredictable, or personal security is a significant concern.

Once the ordinary and necessary requirement is met, the next issue is to determine which costs are deductible and which are not. If the aircraft is owned by an entity other than a single-member limited liability company (SMLLC) owned by an individual, costs need to be apportioned to each passenger on each flight and then allocated between business and personal. Personal flights can further be broken down between personal non-entertainment and personal entertainment. For purposes of determining the expenses allocated to entertainment air travel of a specified individual, a taxpayer must use either the occupied seat hours or miles, or the flight-by-flight method. A taxpayer must use the chosen method for all flights of all aircraft for the taxable year. Taxpayers should quantify the deductible costs under all allowed methodologies each year to identify the maximum business deductions allowed.

If the aircraft is owned by an individual or through a SMLLC, there is a different allocation methodology to determine which expenses are deductible. Generally, this results in classifying each trip as primarily personal or primarily business. Many factors are used to determine the appropriate classification.



Historically, costs associated with travel to and from a business entertainment event were fully deductible if certain rules regarding the entertainment event were met. The 2017 Tax Act has implemented new rules governing the deductibility of expenses associated with business entertainment. Depending upon the additional guidance issued to support these new rules, there may be an impact on the tax treatment of travel to and from a business entertainment event.

Airplanes

Personal travel using private aircraft

Aircraft can be a useful tool for business travel, easing security concerns, allowing flexibility for changing schedules and maximizing owners' and executives' availability to attend to business matters. However, fairly often the personal usage increases steadily. This creates tax effects that are important to understand. The American Jobs Creation Act of 2004 and its related subsequent regulations have put limitations on the deductibility of aircraft use.

Generally speaking, aircraft use is deductible for business purposes, but it may not be deductible when flown for personal use, depending on the category of the flight. Personal aircraft usage breaks down into two categories: personal non-entertainment and personal entertainment. These categories are only relevant if a regarded tax entity is providing the aircraft to employees, owners, or guests. If the aircraft is being provided from a SMLLC to its owner, the other rules discussed previously will apply.

If a specified individual (generally defined as an owner, shareholder, or officer of a company) flies for personal entertainment purposes, the cost of the flight is only deductible to the extent compensation has been imputed to the individual for the flight or the specified individual reimbursed the company for the cost of the flight. Personal entertainment is broadly defined and generally includes all personal travel that is not otherwise categorized as personal non-entertainment.

Additionally, spousal travel is not deductible, unless the spouse is an employee of the company and is also traveling for business purposes. However, if the spouse's travel can be considered personal non-entertainment travel (i.e., they are traveling as a companion to a business event where spouses are expected or encouraged to attend), income related to the spouse's travel would be imputed to the executive, which could then (in limited circumstances) make the full cost of the travel deductible.

Personal travel is also considered a fringe benefit provided to the employee or owner in which income needs to be imputed to the individual, or reimbursed, for use of the aircraft. Most companies, when imputing income to an executive for personal use of an aircraft, utilize the Standard Industry Fare Level (SIFL) tables. SIFL tables can require an amount of income to be imputed to the individual that is less than the actual cost or fair market value of operating the aircraft. As long as the executive has compensation imputed to him or her for the flight, or reimburses the company an appropriate amount, personal non-entertainment flights can generally be fully deductible by the company. Again, the income imputation requirement is only found when a non-cash fringe benefit is provided to an employee or owner. If a SMLLC is providing aircraft usage to its sole owner, there is no employer/employee relationship and therefore no fringe benefit applies.

Selling your aircraft

Gain or loss on a disposition of an aircraft can be difficult to calculate, as there are differing methodologies for calculating basis on a disposition. It is important that taxpayers understand the various authorities regarding how basis of an aircraft is affected by personal use before finalizing the gain/loss calculations on a disposition of an aircraft.

Additionally, the 2017 Tax Act has eliminated the ability to defer gain under the like-kind exchange rules. Therefore, aircraft will be fully taxable when disposed; however, they are eligible for 100 percent bonus depreciation, as discussed previously.

Yachts

A yacht is another asset that presents unique tax considerations.

Yacht financing

Many of the yachts built in the United States are constructed in Louisiana and Mississippi. Yacht construction resembles home construction in some regards, but there are income tax issues related to construction loan interest that should be considered.

Generally, interest on personal use property is not capitalized. A yacht may qualify as the taxpayer's personal residence, and the loan may be secured by the yacht itself. If so, the interest on a construction loan of a personal residence can be mortgage interest for up to 24 months of the construction phase. In that case, interest deductibility is limited to the same personal residence limitations and is nondeductible for alternative minimum tax purposes. With respect to debt incurred after December 15, 2017, and before January 1, 2026, the reduced limitation on the amount of acquisition indebtedness ($750,000, or $375,000 in the case of married taxpayers filing separately) for the mortgage interest deduction will generally be applicable. Also, the deduction for mortgage interest on home equity indebtedness is suspended for tax years beginning after December 31, 2017, and before January 1, 2026.

When it is delivered to a taxpayer after construction is complete and the yacht passes "sea trials," the seller of the yacht has nexus for state sales and use tax in the state(s) where it has physical presence. However, many "yacht-friendly" states have sales and use tax exemptions for sales with certain load displacements (e.g., 50 tons or more). Although the "selling state" may have an exemption, if the yacht were to cruise in US waters, other states could impose a use tax at their ports if one had not yet been imposed.

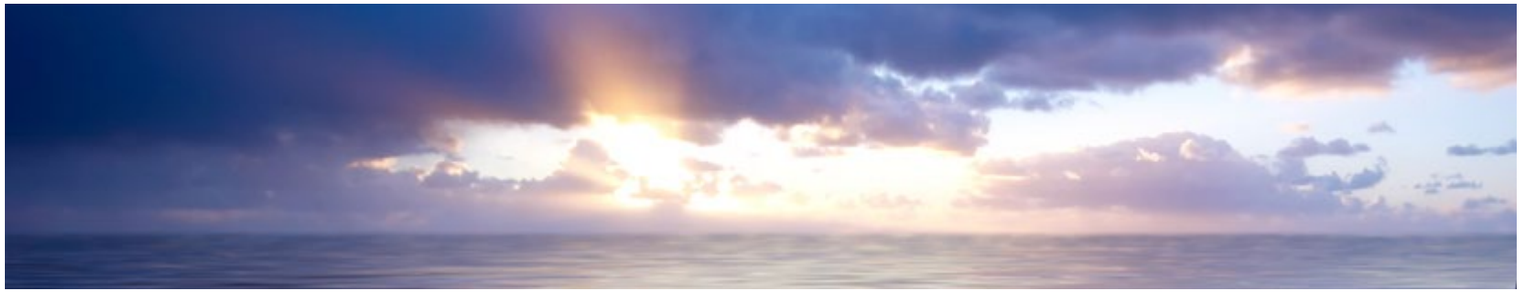
Foreign-flagged vessel (FFV)

There are advantages and disadvantages to becoming an FFV with a US cruising license. Some believe that they may be safer in international waters by not flying the US flag. Also, it may allow for insulation against sales and use taxes imposed by other states.

However, care should be given in selecting the proper jurisdiction. Taxpayers should understand the initial and annual maintenance fees of a foreign registry, which may include registration fees, tonnage fees, company formation, document recording, inspection tariffs, etc. Additionally, it may be seen as detrimental that in order to enter and operate in US waters for pleasure, an FFV must obtain a cruising license, and important restrictions will apply.

Operating costs

Yacht operation is often handled through a management company. For a fee, the management company will handle the crew, maintenance, books and records, and compliance with applicable rules and laws. Yacht operating costs are significant, with annual operating costs typically running 10 percent or more of the acquisition cost.



Yachts

Chartering activities

Chartering may become an appealing option to offset the costs of owning a yacht. Chartering income may be offset by a portion of operating and maintenance costs, as well as depreciation. The management company would handle the details, but it would also take a commission. For an FFV, the yacht cannot be chartered within US waters.

Finally, there are special considerations for the income tax treatment of a yacht that is operated for both personal and charter purposes ("mixed use property").

Determining the deductible portion of yacht expenses is a complicated calculation. The taxpayer should engage tax advisers familiar with these rules to reduce the potential IRS challenges regarding the deductibility of such costs.

Dispositions of yachts

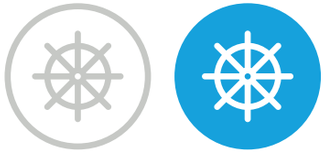
Ultimately, if the investor chooses to dispose of the yacht, then there are additional income tax considerations. If the yacht is chartered, a portion of the related gain, if applicable, is ordinary income to the extent of prior depreciation allowed or allowable. Also, based upon the extent of historical personal use, any prior suspended losses may not be utilized to offset any gain upon sale and are lost. In addition, any loss realized on the sale of the yacht cannot be recognized. If the restrictions for a personal use vessel do not apply, then any passive losses may be "freed up" upon disposition of the activity. It should be noted that an FFV generally cannot be offered for sale in the United States.

Yacht operation: Income tax treatment of mixed use property

Chartering

Question: *Does the high net worth individual charter the yacht to unrelated persons?*

Multiple courts have treated yachts as an "entertainment facility" under section 274. As such, expenses are nondeductible.



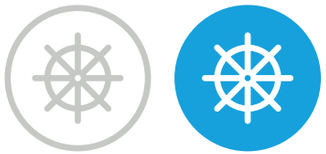
An exception applies for "operating a pleasure cruise ship as a business." Treas. Reg. § 1.274-2(f)(2)(ix).

Chartering will permit an allocable share of expenses to be deductible.

Personal use

Question: *Does the high net worth individual use the yacht for the greater of 14 days or 10 percent of the days chartered?*

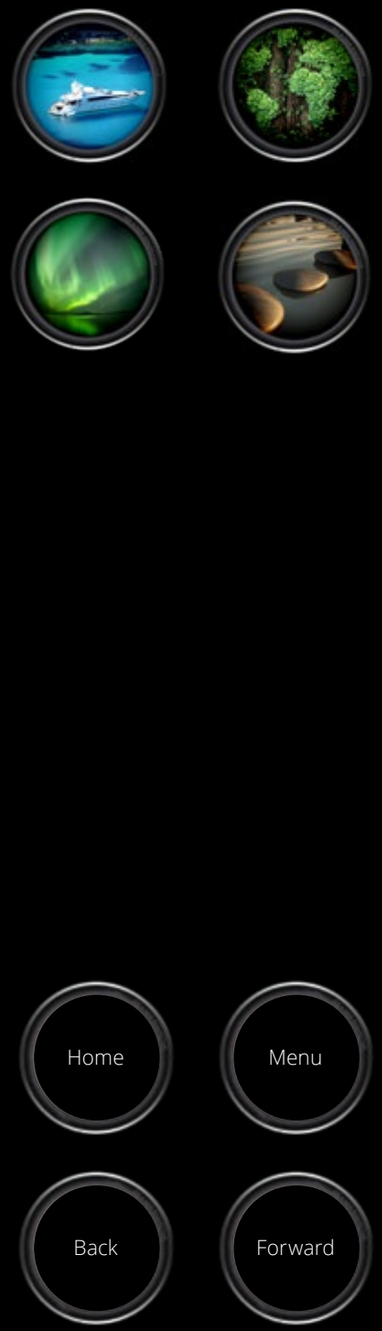
Chartering activity is a section 162 activity but could be subject to the passive activity loss rules under section 469 and may be susceptible to the hobby loss rules under section 183.



Yacht classified as section 280(A) property. Allocable expenses in excess of charter income are not deductible and are carried forward to offset income in future years.

Globalization

“Globalization” may have seemed an abstract and distant term yesterday. Today, with companies and businesses expanding their footprints, workforces, and talent, and investment capital becoming more mobile, globalization is unstoppable. The world we live in is increasingly borderless. It is no longer uncommon to see cross-nationality marriages, members of the same family living in different countries, or individuals living in one country but working in another. Understanding how to manage global tax obligations effectively has become increasingly important for many individuals and families.



Globalization in action

Global migration

Globally, there were **258 million** international migrants in 2017.[1]

Between 1990 and 2017, the number of international migrants worldwide rose by more than **105 million**, or **69 percent**. Much of this growth occurred between 2005 and 2017, when some 5.6 million migrants were added annually, compared to an average of 2.5 million from 1990 to 2005.[1]

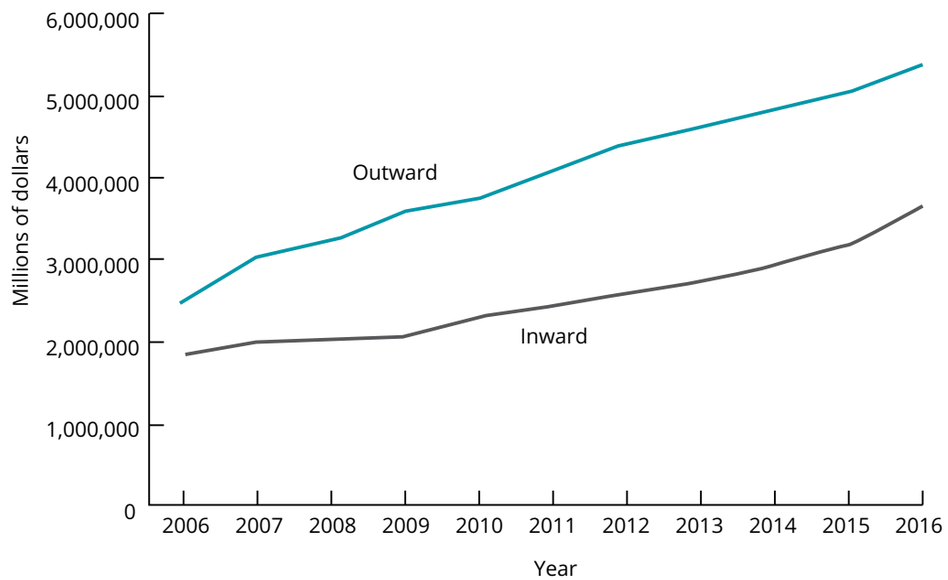
In the United States, more than **1.1 million** persons obtained permanent resident status in 2017.[2]

There were more than **181 million** non-immigrant entries in the United States in 2017.[3]

- More than 3.9 million were temporary workers and their families[3]
- 900,000+ were intracompany transferees[3]
- 470,000+ were treaty traders and investors[3]
- More than 8.4 million were temporary visitors for business[3]

Direct investment and activities of multinational enterprises

In 2016, the US direct investment position in all countries (outward) was $5.3 billion, an increase of 5.6 percent from 2015. The direct investment position from all countries in the United States (inward) was $3.7 billion, an increase of 12.8 percent from 2015.[4]



1 http://www.un.org/en/development/desa/population/migration/publications/migrationreport/docs/MigrationReport20157.pdf
2 https://www.dhs.gov/sites/default/files/publications/Yearbook_Immigration_Statistics_20157.pdf
3 US Department of Homeland Security
4 Bureau of Economic Analysis—US Department of Commerce

Key questions to ask in a global context

If you and your family are thinking of joining the globalization trend and moving and/or investing internationally, consider these questions:

- How will you manage investment, legal, immigration, tax, and accounting issues?
- What types of investment vehicles should you consider?
- Should potential estate taxes or inheritance taxes affect the structuring of your international investments?
- What are some of the tax considerations for non-US families making US investments?
- What are the potential issues for US families making investments in foreign countries?
- What effect does family mobility have on investment planning and taxation?
- Do you understand how to comply with your US and foreign country tax obligations?
- Do you know what your overall tax position will be across the globe?

Cross-border income tax considerations

Inbound considerations

If you are not a US citizen and you are moving to or investing in the US, how you are taxed is determined by your residency status.

Obtaining a green card is one way to establish US residency. The other way is to meet the substantial presence test. The substantial presence test is defined as being physically present in the US at least:

- 31 days during the current year, and
- 183 days during the three-year period that includes the current year and the two years immediately preceding the current year, by adding together the following:
  - All the days you were present in the US in the current year
  - One-third of the days you were present in the first year before the current year
  - One-sixth of the days you were present in the second year before the current year.

Once you become a US resident, you will be subject to US tax on your worldwide income in the same way as a US citizen. You may still have significant economic ties in your home country (for example, bank accounts, investments, stock holdings in companies, pensions, trusts). The US has certain "anti-deferral" rules and some of those investments, although they may be tax-favorable in a foreign jurisdiction, could give rise to adverse US tax consequences. You will also need to be aware of the various US information reporting obligations that may apply, as failure to fulfill these obligations could result in significant penalties. The 2017 Tax Act[1] has layered on additional complexities in this arena, some of which had immediate impact for tax year 2017, while additional changes were enacted prospectively.

Anyone who is not a US resident is referred to as a "nonresident alien." As a nonresident alien you are generally taxed in the US on income from US sources. In some circumstances, even if you meet the substantial presence test, you may be treated as a nonresident alien due to the application of certain exceptions or by application of an income tax treaty between the US and a foreign country.

Once you become a US resident, you will be subject to US tax on your worldwide income in the same way as a US citizen.

1 An Act to provide for reconciliation pursuant to titles II and V of the concurrent resolution on the budget for fiscal year 2018.

Cross-border income tax considerations

Most of the individual states in the US impose income tax. Some cities and localities also impose income tax. Given that states have varying definitions of residency, tax rules, and tax rates, it is important to understand the tax rules for the state you are moving to or investing in. Generally, if you are a tax resident in a state, you are taxed in that state on your worldwide income. If you are a nonresident, you are taxed only on your income sourced from the state.

Once you have moved to or invested in the US, what happens back home? What is your residency status in your home country? Will you need to continue paying tax or filing tax returns there? If you are required to pay tax in both your home country and the US, will you be taxed twice? Does the domestic legislation in the US or in your home country provide relief for double taxation? Is there an income tax treaty between the US and your home country? Does the state you are moving to or investing in give you the benefit of the tax treaty at the state level?

There are many issues to consider when you want to move to or invest in the US. Various actions that you take may affect the amount of taxes you pay in the US and your reporting obligations. Tax planning, therefore, is not only essential from a US tax perspective but also crucial in determining a tax-efficient global tax position.

Outbound considerations

If you are a US citizen or a green card holder, you are subject to US tax on your worldwide income regardless of where you live. Your US filing and reporting obligations do not stop when you move to a foreign country. On the contrary, they tend to become more complex.

If you establish a business or make investments in a foreign country, you may have additional information reporting obligations in the US. US tax rules may also disadvantage some types of investments and entity structures. It is therefore important to consult with your tax advisor before you take action in order to understand the potentialtax consequences and possible tax-efficient alternatives.

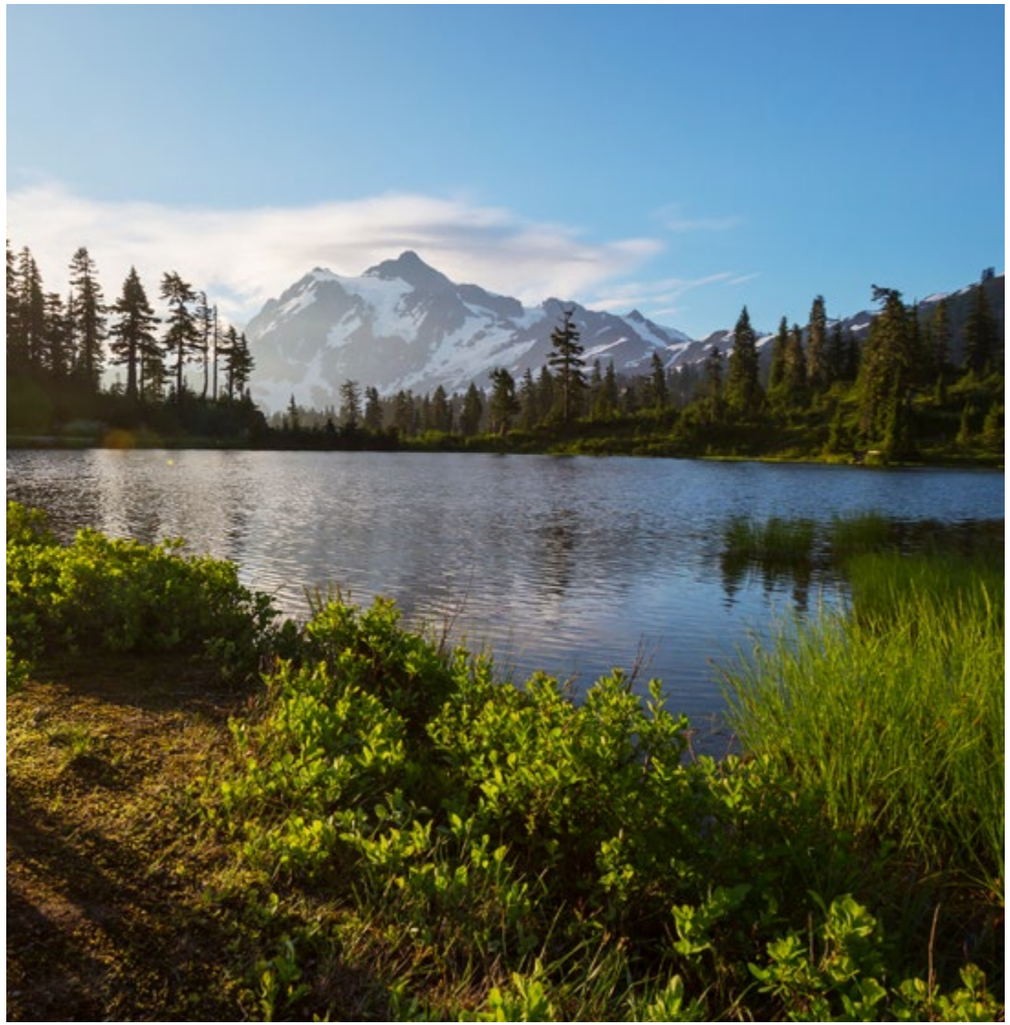
You may establish residency and be subject to tax in a foreign country. The foreign country may provide relief for double taxation in their domestic legislation or have an income tax treaty with the US, which may also help reduce double taxation. However, the foreign country may tax your US investments differently, and there may still be situations in which you are taxed twice if appropriate planning has not been implemented.

Cross-border income tax considerations

If you are leaving the US and you do not hold a green card or US citizenship, you may cease being a US resident in the year of departure or the year after your departure if your later trips back to the US are minimal (that is, no longer meeting the substantial presence test). You may still have US filing obligations after you become a nonresident alien if you receive US effectively connected income (ECI)—that is, income arising from the activities of or assets used in a US trade or business. Examples of ECI include compensation for personal services performed in the US, income and profits from the operation of a business in the US, and income from the disposition of US real property. Certain other types of income may be subject to US income tax, but the tax may be satisfied by withholding (e.g., dividends from a US corporation).

Surrendering your green card will cause you to be considered a nonresident alien for US income tax purposes. If you subsequently spend substantial time in the US (after surrendering your green card), you may again become a US resident under the "substantial presence" test. Upon surrendering your green card, you will need to consider whether you are subject to the US expatriation tax or "exit tax."

As mentioned earlier, states have varying rules, and it is equally important to understand the state tax implications when you move out of the US.



Estate and gift tax considerations

Whether and how your assets are subject to US estate and gift taxation depends on your domicile status.

Domiciliaries

Determining domicile for US estate and gift tax purposes is different than determining US income tax residence discussed in the previous section. You are considered to be domiciled in the US for estate and gift tax purposes if you live in the US and have no present intention of leaving. Thus, you may be a resident for income tax purposes, but not US domiciled for estate and gift tax purposes.

Facts and circumstances test

To determine whether you are a US domiciliary, the following factors are considered:

- Statement of intent (in visa applications, tax returns, will, etc.)
- Length of US residence
- Green card status
- Style of living in the US and abroad
- Ties to former country
- Country of citizenship
- Location of business interests
- Places where club and church affiliations, voting registration, and driver's licenses are maintained

For details on how US estate and gift tax applies to you as a US domiciliary, please refer to the "Wealth transfer planning" section of first installment of this guide.

It is possible that two or more countries will consider you a domiciliary, and/or that certain assets may be subject to estate or gift tax in more than one country.

As of January 2018, the US has entered into estate and/or gift tax treaties with 16 jurisdictions. Tax treaties may define domicile, resolve issues of dual-domicile, reduce or eliminate double taxation, and provide additional deductions and other tax relief.

Countries with whom the US currently has gift and/or estate tax treaties

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

*Through the income tax treaty

Estate and gift tax considerations

Non-US domiciliaries

You are considered a non-US domiciliary for estate and gift tax purposes if you are not considered a domiciliary under the facts and circumstances test described on the previous page.

As a non-US domiciliary you are taxed only on the value of your US situs tangible and intangible assets owned at death, and on the value of your US situs tangible assets gifted during your lifetime, with a maximum tax rate of 40 percent. An exemption of $60,000 is available, but only for transfers at death. US situs tangible assets generally include real and tangible personal property located in the US and business assets located in the US; US situs intangible assets include stock of US corporations. The definition of US situs assets may be modified by an applicable estate and/or gift tax treaty.

US citizens with noncitizen spouses

There are additional estate and gift tax considerations when only one spouse is a US citizen.

An unlimited amount can be gifted to a spouse who is a US citizen, whereas gifts to a noncitizen spouse are offset by an increased annual exclusion ($152,000 for 2018, indexed annually). US citizens and domiciliaries can also "gift split," allowing married donors to exclude up to $30,000 per donee per year (for 2018, indexed annually). Gift splitting is not permitted if either spouse is a non-US domiciliary.

When both spouses are US citizens, an unlimited amount of assets can pass between them without being subject to US estate tax. An election can also be made on a timely filed estate tax return to pass any remaining exemption amount to the surviving spouse for use in addition to his or her own exemption. If your surviving spouse is not a US citizen, the marital deduction is generally not allowed. However, a deferral of US estate tax for assets passing to a noncitizen surviving spouse may be obtained if US property passes through a qualified domestic trust. Some estate and gift tax treaties also allow for some form of a marital deduction in cases where such a deduction would not normally be available.

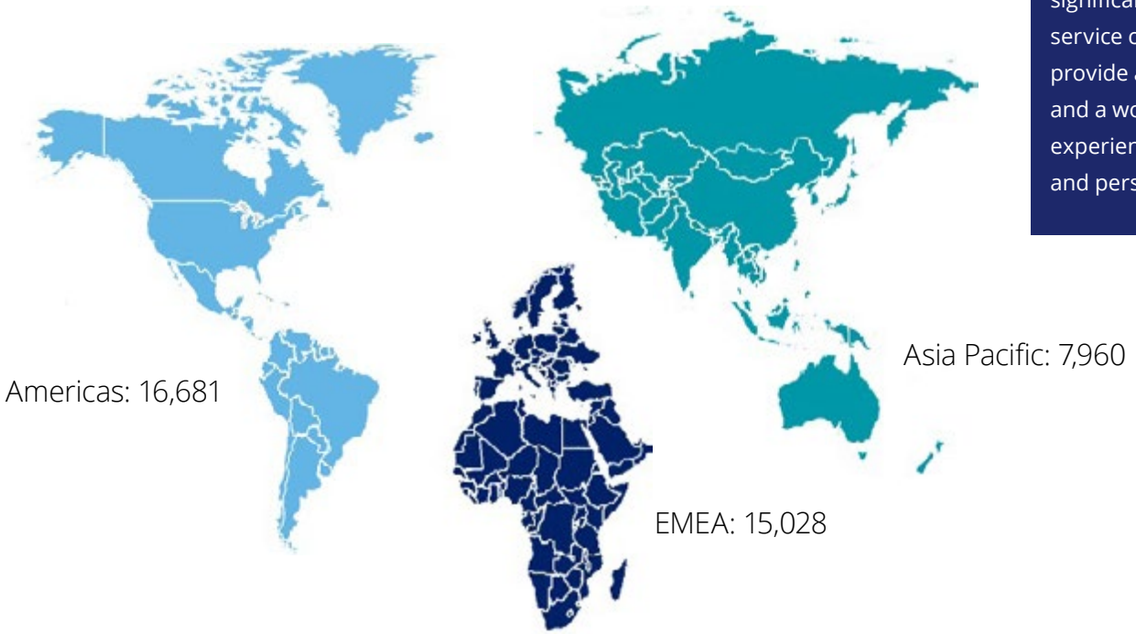
As a non-US domiciliary you are taxed only on the value of your US situs tangible and intangible assets owned at death, and on the value of your US situs tangible assets gifted during your lifetime, with a maximum tax rate of 40 percent.

Thinking ahead

As companies and individuals are increasingly globally mobile, more and more people will be affected by multinational tax rules. Individuals and families moving and/or investing internationally need to have a clear understanding of the potential tax implications. Before taking action, it is important to seek professional tax advice in order to understand how your US tax obligations interact with foreign country tax obligations and what your global tax position will look like.

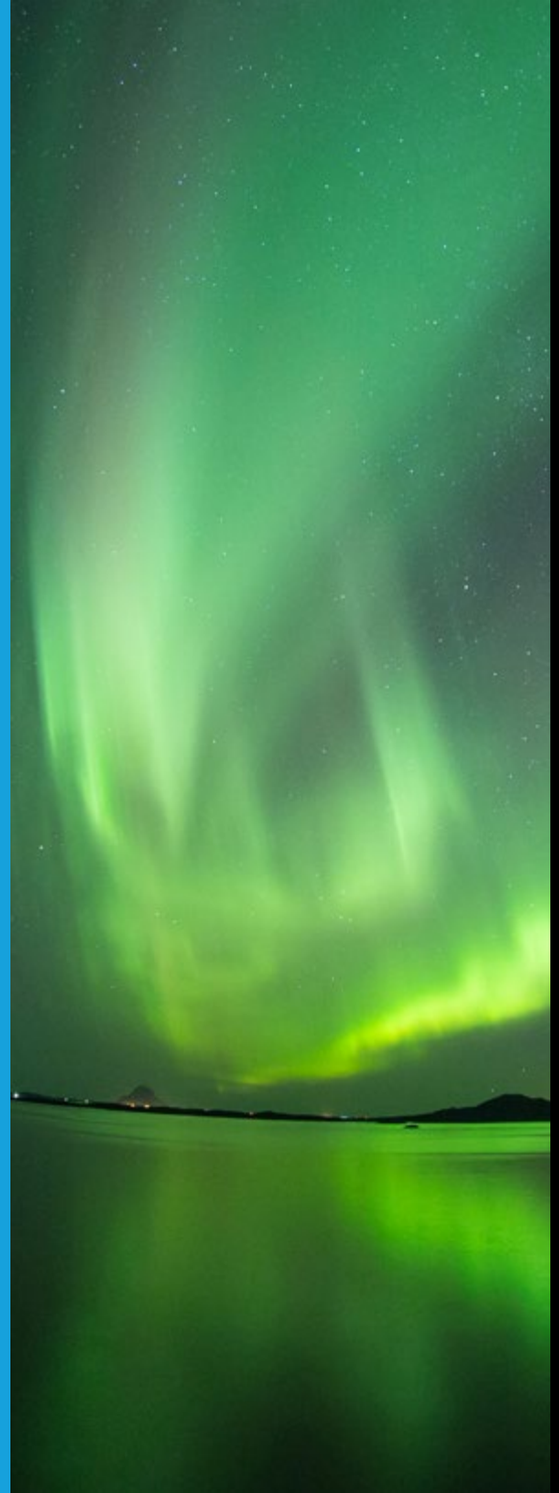
How Deloitte can help
Nearly 40,000 tax professionals globally

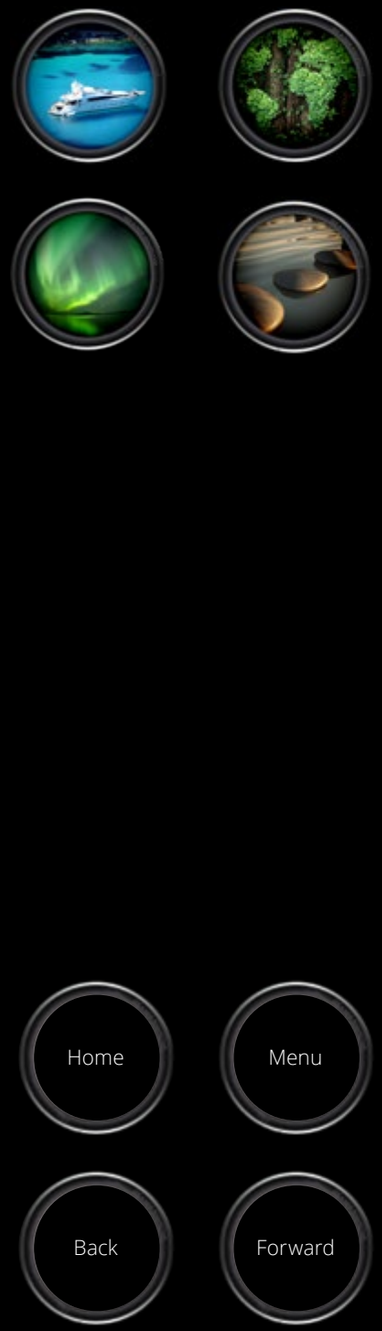
Deloitte has been discreetly serving high net worth individuals, families, and their enterprises for more than 100 years. As a trusted adviser to many of the world's most affluent families, family offices, and private trust companies, we bring significant experience and integrated service capabilities to our clients. We provide a global network of resources and a world-class level of knowledge and experience tailored to each family's unique and personal circumstances.



Cryptocurrencies

Cryptocurrencies are virtual currencies that use encryption techniques to regulate the generation of units of currency and verify the transfer of funds. Cryptocurrencies operate independently of a central bank or similar institution; instead, they employ a decentralized ledger system built on blockchain technology. In other words, network participants self-regulate on a peer-to-peer basis rather than rely on a trusted third party.





What are cryptocurrencies?

An entity creates a cryptocurrency by solving complex cryptographic algorithms (e.g., SHA-256) to arrive at the representation of one unit of value, such as a coin or token.

Cryptocurrency coins and tokens have come into their own as an asset class and are becoming an increasingly popular topic in wealth planning discussions. A person may take possession of cryptocurrency through a variety of means, including purchasing them through an exchange; indirectly, by investing in a private equity fund; and receiving them as compensation for employment, to name a few examples. A person may also be a participant in a cryptocurrency network as a miner, solving computations and supporting the network in exchange for the reward of additional cryptocurrency.

Income tax considerations

Presently, there is a dearth of formal guidance from US government regulators. The only guidance from the Internal Revenue Service (IRS) to date is IRS Notice 2014-21, whereby the IRS has stated that virtual currency is treated as property for federal tax purposes. The guidance, while helpful, addresses a very limited number of issues. What many cryptocurrency holders and their advisers are discovering is that the tax treatment of transactions involving cryptocurrency is much more complex than the tax treatment of more traditional assets such as stock and securities.

The federal government has yet to inform the public which agency or agencies will regulate cryptocurrencies and when it will issue regulations that will provide the information needed to report cryptocurrency transactions. As a result, cryptocurrency exchanges are only slowly starting to provide tax documents like 1099-K forms to traders, and the accuracy of these documents is open to debate.

For the unwary taxpayer, a number of pitfalls may exist. One common mistake is the belief that exchanging cryptocurrency for cryptocurrency is not taxable until ultimately converted to fiat (e.g., USD). The exchange of cryptocurrency for anything (e.g., other cryptocurrency, property, or services) is a recognition event for tax purposes. This oversight can cumulatively result in a significant and sometimes unidentified tax liability to the extent of gain on those transactions, particularly for active cryptocurrency traders. Another problematic area is the misapplication of section 1031 like-kind exchanges to cryptocurrency. Cryptocurrency in almost all cases does not qualify as property for like-kind exchanges under the section 1031 framework, and assertions to the contrary—both now and in prior years—could result in tax positions that are costly and onerous to unwind.

Note that in IR-2018-71, the IRS reminds taxpayers that income from virtual currency transactions is reportable on their income tax returns. Further, the IRS recently indicated that it is concerned about the failure to report capital gains related to cryptocurrencies and some business use of cryptocurrency to pay employees and to buy and sell goods.

It is important to think through these and many other issues when investing in cryptocurrencies. Getting the appropriate tax advice is essential to avoid pitfalls and stay compliant with your tax obligations.

- How should you track your basis?
- How should you treat the chain split coins and air-dropped tokens?
- Do you need to file an FBAR if you trade on a foreign exchange?
- What happens if you donate cryptocurrencies to charities?
- How are cryptocurrency loans taxed?
- What kind of investment vehicles should you use?
- Do wash-sale rules apply?
- What happens if you lose your key or access to your wallet?

Estate and gift tax considerations

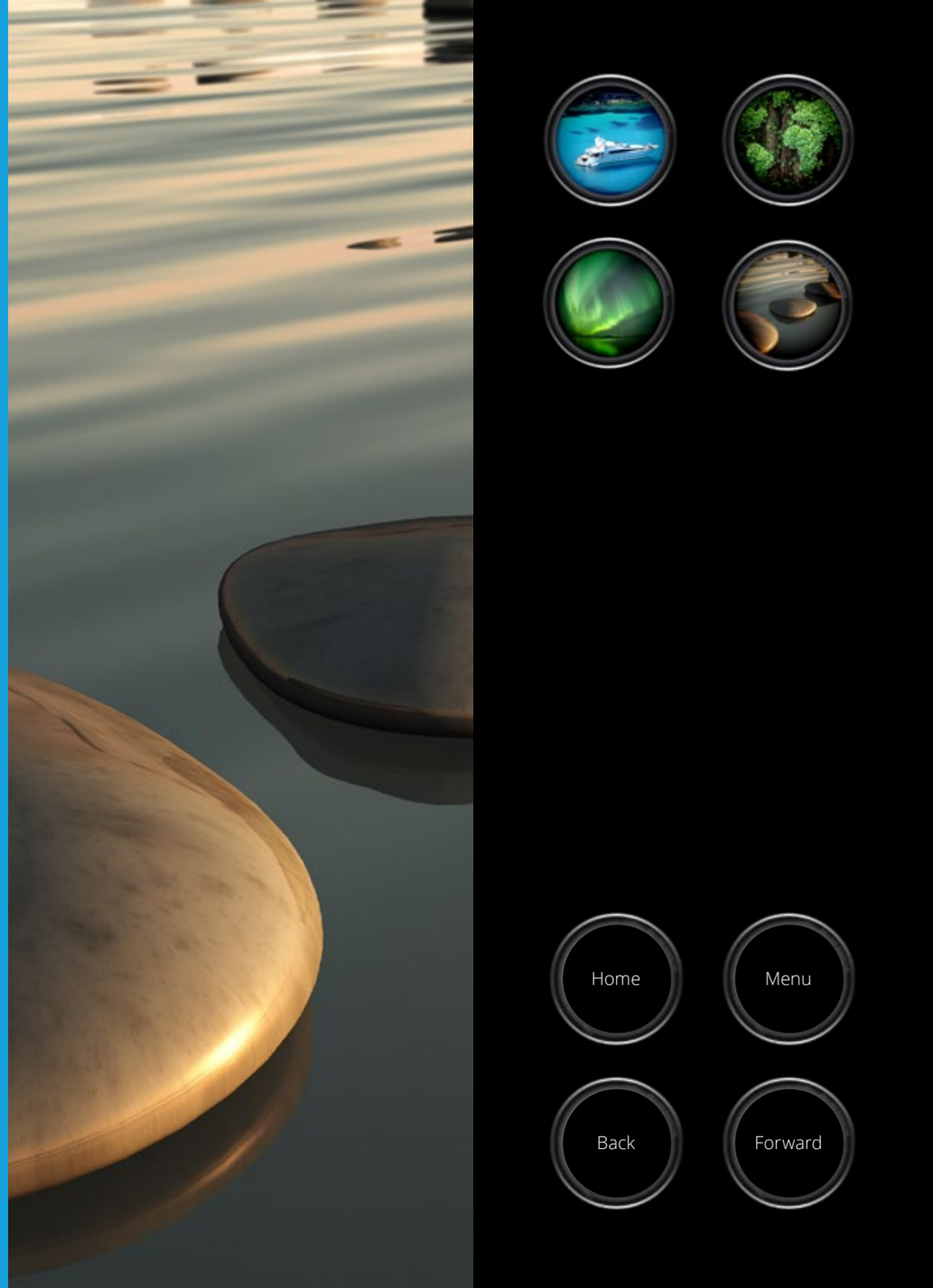
With the increasing amount of wealth generated from cryptocurrencies, estate and gift tax planning involving cryptocurrencies has become a hot topic.

Due to the high volatility of cryptocurrencies, planning techniques like simple transfers to irrevocable grantor trusts may not be appropriate. On the other hand, a grantor-retained annuity trust, or a charitable remainder trust (especially for young players in the cryptocurrency world who do not yet have heirs), may be more attractive.

There are many considerations when it comes to estate and gift tax planning involving cryptocurrencies. Advisers should consider estate and gift tax planning in conjunction with income tax planning tailored for each individual's or family's situation.

Tax policy update

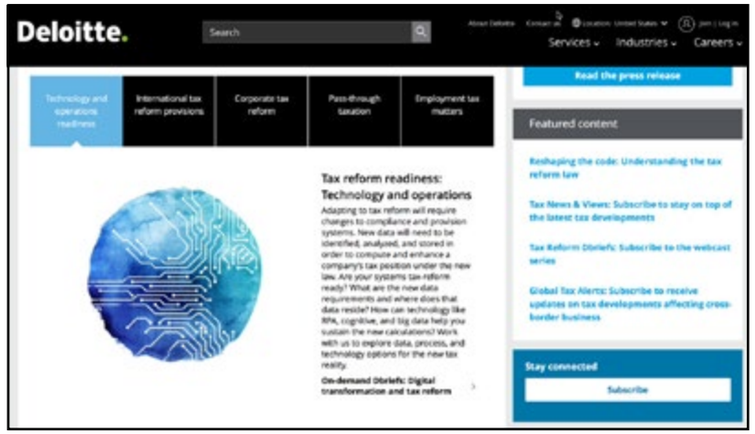
As taxpayers close out the first full year under the 2017 Tax Act,[1] 2018 tax return preparation and forward-looking planning will likely feature a new set of challenges. The tax environment continues to evolve, and the IRS and Treasury have yet to finalize guidance on key provisions. In this landscape of lingering uncertainty and prospective opportunity, vigilant tracking and attentive management of tax issues are likely to remain priorities.



1 An Act to provide for reconciliation pursuant to titles II and V of the concurrent resolution on the budget for fiscal year 2018.

From reform to reality

Eventually, the current tax reform ambiguity will become your tax reality. What you do now—the planning, decisions, and actions you take—can put you, your family, and your business interests in the best possible position to cope with changes to the tax code.



Having access to relevant and timely information, insights, and assistance is key to navigating the path ahead. Deloitte Tax has assembled a broad array of resources and perspectives on its new tax reform hub on Deloitte.com. In this one destination, you'll find:

- **The latest tax developments and featured insights**—including updates on IRS and Treasury guidance, Dbriefs webcasts for tax executives, and access to our newsletters and alerts
- **Deep dives on tax law changes and their potential implications**—from international, federal, and state provisions to pass-through taxation to technology and operations
- **Industry-specific perspectives on tax reform readiness**—across life sciences and health care; technology, media, and telecommunications; and financial services

Tax reform resources

Tax News & Views
Stay ahead of tax reform and other tax policy developments. Our Tax Policy Group publishes a regular newsletter called *Tax News & Views*, which offers clear, concise, and timely coverage of the significant tax developments on Capitol Hill and what they mean for taxpayers.

Visit www.deloitte.com/us/taxnewsviews.html to subscribe to *Tax News & Views* and have the latest tax reform developments sent to your inbox.

About our Washington National Tax practice
Deloitte's Washington National Tax (WNT) practice is a select group of tax specialists whose knowledge, skill, and experience bring world-class insights to our tax leader clients. Our teams include former high-ranking Treasury and IRS officials, congressional staff, state officials, and other professionals with considerable private sector and industry experience. This group uniquely positions Deloitte to help you identify opportunities, respond proactively to changes in the tax environment, and develop adaptable positions for sustainable advantage.

Dig deep into issues that matter to you

Entity conversion

- Should you retain your pass-through status or consider converting to a C corporation? Explore the implications of tax reform on your pass-through entity: Tax reform pass-through impacts
- Read our chapter on Choice of entity and addressing entity conversion considerations in the second installment of the *2018 Essential tax and wealth planning guide.*

Proposed regulations for pass-throughs under section 199A

- Read Deloitte Tax's detailed summary of the proposed regulations issued by the Treasury and the IRS in August that addresses the 20 percent deduction for certain pass-through income under section 199A (enacted in the 2017 Tax Act).

Resources

Unique investments	Art & Finance: Art is your passion...Tax is ours Art & Finance Report 2017 Private aircraft: Flying private makes sense for those with the right information
Cryptocurrency	Classification of cryptocurrency holdings Bitcoin
Globalization	US estate and gift taxation of resident aliens and nonresident aliens Tax planning for US individuals living abroad—2016 Global Employer Services Cross-Border Tax
Tax policy update	Deloitte tax reform hub *Tax News & Views* newsletter

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