GUIDEBOOK ON U.S. TAXATION OF FOREIGN INDIVIDUALS

Charles (Chuck) Rubin,
Attorney at Law
Gutter Chaves Josepher Rubin Forman
Fleisher Miller, PA
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2101 NW Corporate Blvd., Ste 107
Boca Raton, FL 33431
561-998-7847
crubin@floridatax.com
www.floridatax.com
www.rubinontax.blogspot.com

BIOGRAPHY

Charles (Chuck) Rubin
561-998-7847
www.floridatax.com
www.rubinontax.blogspot.com
crubin@floridatax.com

Charles (Chuck) Rubin, a board certified tax attorney, is managing partner of Gutter Chaves Josepher Rubin Forman Fleisher Miller PA, a tax, trusts, and estates boutique law firm situated in Boca Raton, Florida. He is an ACTEC and STEP fellow, and a former adjunct professor at the University of Miami School of Law. Mr. Rubin has published numerous treatises, manuals, and articles, including two BNA Tax Management portfolios, and articles in Journal of Taxation, Estate Planning, Tax Management Estates, Gifts and Trusts Journal, and Tax Notes. He is a regular contributor to Leimberg Information Services. He also authorizes a popular tax blog at www.RubinonTax.blogspot.com, speaks regularly at professional meetings and conferences, is frequently quoted in national publications such as the Wall Street Journal, and was named 2015 & 2017 Attorney of the Year by Best Lawyers in Tax Law for the Miami metropolitan region

Mr. Rubin has received favorable peer ratings and recognition by various publications and rating services, including Best Lawyers, Chambers USA, Martindale-Hubble, Who's Who in America Law, Top Lawyers in the South Florida Legal Guide, SuperLawyers and Florida Trend's Florida Legal Elite, and his firm has a Tier 1 ranking in the U.S. News & World Report Best Law Firm rankings.

PRESERVING AND ENAHNCING INDIVIDUAL, FAMILY AND BUSINESS WEALTH THROUGH:

- Planning to Minimize Taxes (U.S. & International)
- Estate Planning, Charitable, Marital and Succession Planning
- Business Structuring and Transactions
- Trusts & Estates Administration
- Creditor Protection
- Trust, Estate & Tax Litigation and Disputes

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INTRODUCTION 4
INCOME TAXES - CITIZENSHIP AND RESIDENCY 6
INCOME TAXES - NONBUSINESS INCOME 8
INCOME TAXES - BUSINESS INCOME 9
INCOME TAXES - CAPITAL GAINS AND REAL PROPERTY GAINS 10
INCOME TAXES - LOCAL AND STATE TAXES 11
ESTATE TAXES 12
GIFT TAXES 14
GENERATION SKIPPING TAXES 15
REPORTING REQUIREMENTS 16
PENALTIES AND ENFORCEMENT 18
TAX PLANNING 19

INTRODUCTION

The U.S. taxes foreign persons on their income and assets related to the U.S. Foreign persons who are *also* citizens, residents, or domiciliaries of the U.S. are generally subject to greater U.S. taxes than other foreign persons.

The rules of taxation in this area are complex and confusing. This Guidebook is intended to provide a basic understanding of those rules. It is not intended to substitute for the guidance of qualified tax counsel - however, it should go a long way in making such guidance more understandable and meaningful to the reader.

There are two general areas of U.S. tax that should concern a foreign person. The first is income taxes - taxes on income earned by the foreign person. The second is transfer taxes on gratuitous transfers. This second area is transfer taxes - estate taxes (taxes on the value of property transmitted by an individual at his death to his successors in interest), gift taxes (taxes on the value of property given by an individual during his lifetime to other persons), and generation-skipping taxes (gratuitous transfers that skip one or more generations). Each general area has its own rules and tax rates.

These taxes are federal taxes. Additionally, states and local governments may impose similar taxes, but usually at lower rates. There are many other taxes imposed in the U.S., including employment and social security taxes, real estate and other ad valorem taxes, excise taxes, and sales and use taxes - all of which may at times apply to foreign persons. Value added taxes are not generally imposed. These other taxes are not discussed in this Guidebook.

The principal agency of the Federal Government for tax collection and enforcement is the Internal Revenue Service. State and local governments have their own

tax agencies - one example is the Florida Department of Revenue for the State of Florida.

The U.S. tax system is based largely on voluntary compliance. Taxpayers prepare tax and information returns by themselves. Then, they submit them to the tax authorities with the appropriate tax payments. Tax authorities review this voluntary system with audits of taxpayers. In an audit, the Internal Revenue Service examines the tax returns, books and records of a taxpayer to determine if the taxpayer complied the law. The Internal Revenue Service may increase or decrease the tax due and impose penalties.

Residents of countries with tax treaties with the U.S. may receive more favorable U.S. tax treatment than residents of non-treaty countries. These treaties can vary some of the general rules discussed in this Guidebook.

This Guidebook is limited to U.S. taxes on individuals. Separate taxation regimes apply in the income tax area to the taxation of corporations, partnerships, and other entities.

INCOME TAXES - CITIZENSHIP AND RESIDENCY

The U.S. taxes its *citizens* and *residents* on their world-wide income. Individuals who are *not* citizens or residents of the U.S. are generally taxed only on their income from U.S. sources. Therefore, for purposes of U.S. income taxes, foreign individuals usually desire to avoid U.S. citizenship and U.S. residency (that is, they usually desire to be "nonresident aliens"). However, since U.S. citizens and residents will usually receive a tax credit for income taxes paid to other countries up to the rate of tax imposed by the U.S., becoming a U.S. citizen or resident may not result in overall higher worldwide taxation.

It is important for a foreign person to know the basic rules that determine his income tax status. Generally, an individual is a U.S. *citizen* only if born or naturalized in the U.S., or has U.S. citizen parents. Questions regarding citizenship for income tax purposes are generally resolved by U.S. immigration law. Individuals should consult with an immigration attorney to resolve questions concerning U.S. citizen status.

Even though an individual is not a U.S. citizen, he or she can still be a U.S. *resident*. Generally, such a person will be a resident only if (a) such individual has lawful permanent resident status for U.S. immigration purposes (*i.e.*, the individual possesses a "green card"), or (b) such individual spends so much time in the U.S. that he or she is deemed a resident under the "substantial presence" test. Additionally, residency can result when the individual makes an affirmative election to be treated as a U.S. resident in the year prior to which he or she satisfies the substantial presence or files a joint return with his or her U.S. resident spouse for the tax year.

Under the "substantial presence" test, an individual who spends 183 days or more in the U.S. during a calendar year will generally be considered a resident. In counting days present in a given year, the individual must add to the total number days present in the given year 1/3 of the days present in the preceding calendar year and 1/6 of the days present in the second preceding calendar year.

EXAMPLE: Carlos Rivers was present in the U.S. 110 days in 2013, 120 days in 2012, and 240 days in 2011. His total days present in 2013 for this purpose are 190, computed as follows:

1993	110 days
1992 (120/3)	40 days
1991 (240/6)	40 days
	190 days

Thus, Carlos will be considered a U.S. resident for income tax purposes in 2013.

Under the substantial presence test, special rules may exclude certain days present from being counted. Also, if the individual is present in the U.S. for fewer than 183 days and can establish a closer connection to another jurisdiction, U.S. residency can be avoided. A useful guide in this area is an individual can usually avoid resident status by spending no more than 120 days in the U.S. in each year.

INCOME TAXES - NONBUSINESS INCOME

The U.S. imposes a thirty percent withholding tax on certain nonbusiness income paid to nonresident aliens from U.S. sources. Technically, this income is referred to as U.S. source income that is "fixed or determinable, annual or periodic." It includes U.S. source:

A. interest income;
B. dividend income;
C. rental income;
D. compensation income that is not effectively connected with a U.S. trade or business;
E. annuity income; and
F. certain other similar types of income.

Generally, the U.S. payor of such income must withhold the tax from the payment to the nonresident alien. However, if no such withholding occurs, the nonresident alien is required to pay the tax. Special rules determine when such income is from U.S. sources. Also, special exceptions from taxation apply. A principal exception is for interest paid on deposits with U.S. banks and savings and loan associations. Interest on certain portfolio debt obligations may also be exempt from this tax at times.

If such income is also characterized as income effectively connected with a U.S. trade or business, as explained below in the Section "Income Taxes - Business Income," this thirty percent withholding tax will not apply. Instead, the income will be taxed as explained in that Section.

INCOME TAXES - BUSINESS INCOME

A nonresident alien that (a) is engaged in a U.S. trade or business, and (b) has income that is effectively connected with that U.S. trade or business, will be taxed on that income in the same manner as a U.S. person. That is, the U.S. will tax the nonresident alien of such income at graduated rates after the income is reduced by deductions related to such income. Combined federal and state income taxes can exceed 39%.

Generally, a nonresident alien will be considered to be in a U.S. trade or business if he or she conducts relatively continuous business activities from a fixed location in the U.S. Most U.S. source income arising in that business will be considered "effectively connected" income, and some foreign source income will also be considered "effectively connected."

Determining the existence of a U.S. trade or business or effectively connected income, and the allocations of deductions to that income, can be a complex and difficult task.

INCOME TAXES - CAPITAL GAINS AND REAL PROPERTY GAINS

Generally, the U.S. does not tax nonresident aliens on their gains from the sale of a capital asset. Three principal exceptions to these rules are:

A. Such asset is used in a U.S. trade or business of the nonresident alien;
B. The nonresident alien is present in the U.S. in the year of disposition for 183 days or more; or
C. The capital asset is a U.S. real property interest.

Generally, a U.S. real property interest is vacant land, office buildings, houses, or condominiums, located in the U.S. At times, stock in a U.S. corporation or partnership can also be a U.S. real property interest. If the sale is a sale of U.S. real property interest, under the "FIRPTA" rules the buyer of the property may be required to withhold fifteen percent (ten percent for certain residential property) of the purchase price and pay the withheld amount to the Internal Revenue Service. This payment is a deposit towards any of the seller's taxes arising from the sale. Any withholding more than the tax due will be refunded by the Internal Revenue Service. There are a number of exceptions to this FIRPTA withholding requirement.

INCOME TAXES - LOCAL AND STATE TAXES

The preceding discussion describes federal income taxes imposed on nonresident aliens. In addition to federal income taxes, some states impose their own income taxes on individuals. Local governments, such as cities, may also impose their own income taxes. These taxes are generally at rates much lower than the federal tax rates. Typically, but not always, they are payable under the same rules as the federal income taxes, and thus are payable only when federal income taxes are due.

ESTATE TAXES

The U.S. imposes estate taxes on the net value of property owned by a decedent at the moment of his death. If the decedent is a U.S. *citizen* or U.S. *domiciliary*, his "estate" will be taxed on all of the worldwide assets of the decedent. If the decedent is *not* a U.S. citizen and *not* a U.S. domiciliary (*i.e.*, he or she is a "nondomiciliary"), then the estate taxes will apply only to property *with a U.S. situs*. For decedents who are not U.S. citizens, a key determination, therefore, is whether the decedent is a nondomiciliary. Unlike the "residency" test for income tax purposes described above, there is no objective test for making this determination.

Generally, a person acquires a U.S. domicile only if, at the same time, (a) a person resides in the U.S., and (b) has the intent to reside here indefinitely. This is determined on a facts and circumstances basis.

As discussed above, for a nondomiciliary only U.S. situs assets are subject to U.S. estate taxes. Generally, U.S. situs assets include stock in U.S. corporations, tangible personal property and real property located in the U.S., and bonds and other debt instruments issued by U.S. persons. Exceptions from U.S. situs status exists for certain debt instruments issued by U.S. persons and funds held in a U.S. bank or savings and loan association account. Since stock in a non-U.S. corporation is not a U.S. situs asset, a non-U.S. corporation is often used by nondomiciliaries to hold their U.S. situs assets with the anticipation that this arrangement will shield them from U.S. estate taxes.

Usually, the first $60,000 in assets owned by a nondomiciliary will be exempt from U.S. estate taxes. After that, U.S. estate taxes will apply at progressive rates up to a forty percent maximum. However, if the decedent at his death passes his assets outright or in a qualified trust or other qualified arrangement to a surviving spouse who is a U.S. citizen, the U.S. will not impose its estate tax on such assets at the death of the first spouse. If the surviving spouse is not a U.S. citizen, the decedent can achieve the same result by transferring his assets at his death to a "qualified domestic trust" for the benefit of the

surviving spouse.

In addition to the federal estate tax, state and local governments may also impose an estate tax.

GIFT TAXES

The U.S. taxes gifts of property from one individual to another. Generally, it imposes these taxes at the same rates as the federal estate tax. The U.S. taxes U.S. citizens and domiciliaries on gifts of all property wherever situated. It taxes nondomiciliaries only on gifts of U.S. situs property.

The same definition of "domicile" used in the Estate Tax discussion above applies for gift tax purposes. However, a different definition of "U.S. situs" assets applies. For gift tax purposes, intangible assets such as stock in U.S. corporations and U.S. debt obligations are not U.S. situs assets. Thus, a nondomiciliary can gift these assets without gift taxes even though they may be subject to estate tax if owned by that same nondomiciliary at death.

Individuals can make certain gifts without incurring gift taxes. For example, any individual can gift up to $14,000 each year to as many individuals as he or she desires without the U.S. taxing such gifts if the individual makes such gifts in the proper form. Further, a gift from one spouse to a U.S. citizen spouse is not subject to gift tax. If the recipient spouse is not a U.S. citizen, the spouse making gifts can give the recipient spouse gifts of up to $149,000 each year (subject to annual inflation adjustment - $149,000 is the amount for 2017 gifts) without gift taxes.

Note that some gifts to U.S. persons may need to be reported to the IRS, even though the gift itself is not subject to tax.

GENERATION SKIPPING TAXES

The U.S. imposes a generation skipping tax when gratuitous transfers are made that skip one or more generations. The tax can apply to a direct transfer to a lower generation recipient, and can also apply to distributions from trusts to such lower generation beneficiaries.

The tax will be imposed on skip transfers by nonresidents when the transferred property is situated or deemed situated in the United States for gift or estate tax purposes at the time of transfer. Nonresidents are entitled to the same $5.49 million exemption (for 2017) that U.S persons, but effectively have an unlimited exemption for transfers of property not situated or deemed situated in the U.S.

REPORTING REQUIREMENTS AND INFORMATION SHARING

Generally, a nonresident alien must file U.S. income tax returns only if he or she (a) engaged in a U.S. trade or business during the tax year, or (b) received U.S. source income subject to the thirty percent withholding tax but such withholding requirement was not followed by the payor of such income. In many situations, the nonresident alien will be obligated to obtain a taxpayer identification number to use on his or her U.S. tax filings.

If a nonresident alien is required to file an income tax return but does not file, he or she will lose the ability to reduce his or her trade or business income by permitted deductions. In that situation, the U.S. will instead tax the nonresident alien on a gross basis.

Additional return requirements apply for estate tax and gift tax situations. Further, information returns are often required. For example, information disclosing related party transactions with entities engaged in a U.S. business often must be filed.

It is generally advisable that the assistance of a certified public accountant, with particular experience in international tax matters, be obtained for assistance in determining when returns are required and preparing the required returns. A tax attorney can help determine the scope of U.S. taxation and to plan for minimizing such taxation. Often, proper planning can mean the difference between a substantial tax and no or *de minimis* tax.

Information on taxpayers may be exchanged between governments. Such information exchanges may arise from various sources, including under tax and other treaties of the applicable countries, under the Foreign Account Tax Compliance Act (FATCA), and common reporting standard (CRS). For nonresidents, CRS is more an issue than FATCA.

CRS generally requires reporting of ownership between participating countries, which include BVI, Nevis, Jersey, the European Union, Canada, China, and numerous

South and Central American and Caribbean countries. Notably, the U.S. is not a party to CRS, so that the U.S. has become something of an investment haven for those that do not want their investments reported to their home countries. CRS can still be an issue, however, for U.S. investments if the investments are owned through an entity organized or managed in a CRS jurisdiction.

PENALTIES AND ENFORCEMENT

In many countries of the world, taxation is typically a matter of negotiating with the local tax authorities. Corporations and bank accounts in tax havens, and double sets of books, are often established methods of dealing with the tax collector.

Individuals should avoid such tax practices in the U.S. The U.S. will impose additional taxes and interest on those who fail to follow U.S. tax rules. Also, the U.S. may impose penalties for failure to comply with the law. In intentional evasion situations, the U.S. will impose criminal fines and jail sentences. Consequently, it is important for foreign persons to determine the scope of their U.S. tax obligations and to meet those obligations.

TAX PLANNING

This Guidebook has generally limited itself to a discussion of the principal taxes imposed on foreign persons. With proper planning, foreign persons can often minimize or avoid the U.S. taxes discussed in this Guidebook.

NOTE: The purpose of this guide is to summarize for informational purposes only certain tax information of interest to the clients and friends of Gutter Chaves Josepher Rubin Forman Fleisher Miller P.A. Applying the information herein to a specific situation may involve more complex analysis or other tax provisions that are not described herein for the purpose of simplification. The information contained herein is condensed from, and a general summary of, legislation, administrative rulings, and other information, and should not be construed as legal advice or opinion, and is not a substitute for the advice of counsel or an accountant. For further information, please contact us at the above address.