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# Fundamental Financial Planning and Investment Strategies

for Foreign Nationals Living In United States

NEXIA INTERNATIONAL

# Contributors

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*Andrea is also the Chief Compliance Officer and makes certain that the firm remains aligned with SEC regulatory changes. She monitors everyday firm processes and performs audits on procedures to ensure regulatory and operational compliance. Andrea has previously served as a voting member of the firm Investment Policy Committee for four years, vetting out stock selection for client portfolios. Andrea also takes an active role in hiring, training, and mentoring students who participate in the firm Summer Internship Program.*

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# About this report

This document was written by Wolf Group Capital Advisors for foreign nationals who are planning on moving to the United States and will become U.S. tax residents. The purpose is to provide non-U.S. individuals who have either recently moved to the United States or will move in to the United States in the near future with a basic understanding of some of the important planning fundamentals that should be considered prior to moving and making financial decisions. Proper planning and foresight can eliminate unnecessary taxes on your assets and income, reduce time and fees spent on overly complex compliance, and help you avoid costly penalties associated with improper filing and disclosure.

Some of the planning issues that will be discussed include:

- U.S. Income Tax Introduction – Are you a Resident Alien or a Nonresident Alien?
- Balancing Taxation in Multiple Jurisdictions
- Complications to Maintaining Foreign Assets: Foreign Account Tax Compliance Act (FATCA)
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# Introduction

Relocating within your home country has its trials; relocating to another country is not only challenging, but unnerving. Not only are you dealing with the physical difficulties of moving, you are also dealing with a new country; its laws, its cultures, its customs and all the other little quirks that makes any country so unique and wonderful in its own special way.

Moving to the United States is no exception, whether it is for a year, 10 years, or permanently. It doesn't matter whether you are moving for employment, education, or family; it is crucial that proper planning takes place before you physically arrive in the United States.

The first step toward successfully planning for your future involves building the necessary financial foundation to support your needs and goals. For any individual, developing a sound, tax efficient financial strategy that satisfies their goals and is appropriate for their individual circumstances can be a difficult task. This crucial step is one of the easiest, but also possibly the most detrimental, steps to ignore for extended periods of time.

Comprehensive global financial planning creates a strong foundation built upon informed decisions that arrange the intricate parts of your financial affairs together to meet a common goal. This strong foundation will ensure that proper attention is given to the additional complexities that are unique to being a foreign national living in the U.S. and will allow your wealth to be managed in a suitable, sensible and tax-efficient manner.

This paper aims to help foreign nationals moving to the United States become aware of more than just the "normal" considerations to incorporate into their financial planning and investment strategy decisions. Understanding how a foreign national can become a U.S. tax resident and what that means is important in pro-actively avoiding unnecessary pitfalls. The impact of potentially being taxed in multiple jurisdictions, currency fluctuation, pension laws, mandatory U.S. informational reporting association with ownership of non-U.S. assets and so forth also warrants attention. Far too often, we have seen that both the time

demands of career and family in addition to these complexities lead to procrastination and a lack of appropriate planning.

The topics outlined in the following pages will guide you through the fundamental concepts that will help you properly build a strong foundation for your financial plan.

## U.S. Income Tax Introduction – Are you a Resident Alien or Nonresident Alien?

It is important that an individual determines what his/her tax status in the United States will be prior to actually arriving into the U.S. Without proper understanding and planning, the tax consequences can be quite surprising.

The U.S. income tax system is progressive and is one of the most complicated in the world, with over 70,000 pages of laws and regulations. Generally speaking, a non-U.S. citizen is considered an alien. Aliens fall into two categories for tax purposes: 1) resident alien and 2) nonresident alien. In order to determine your U.S. tax status, you must pass one of the two residency tests (green card test or the substantial presence test), to be considered a resident for income tax purposes in the calendar year.

*Green Card Test*

The green card test is satisfied if a person has obtained lawful permanent resident status under U.S. immigration laws. A person who obtains lawful permanent resident status is considered a U.S. tax resident alien from the first day of physical presence in the Unites States under that status.

*Substantial Presence Test*

Even though an individual does not possess a green card, he/she can still become a U.S. tax resident alien under the “substantial presence test.” This test is based on a person’s physical presence in the United States. The test is satisfied if a person’s days of physical presence within the United States equal or exceed 183 days over a three-year period. The formula is as follows:

| All days of U.S. presence in current year | + | 1/3 of days of U.S. presence for the 1st preceding year | + | 1/6 of days of U.S. presence for the 2nd preceding year |
|---|---|---|---|---|

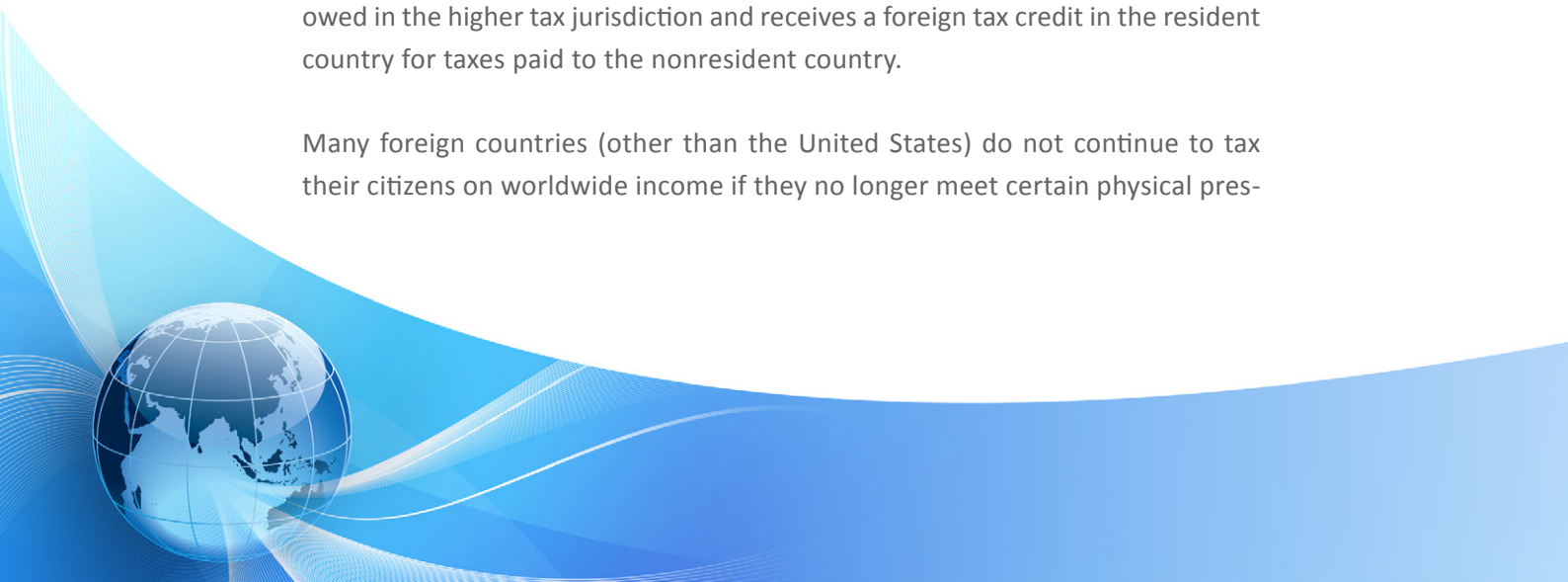
Under this test, a person is generally considered to be a U.S. tax resident alien from his/her first day of physical presence in the United States in the year in which the substantial presence test is satisfied. Generally, there are three levels of taxation in the U.S.: 1) federal level, 2) state level and 3) local level, although this may vary at the state and/or local level. For purposes of this document, we will only highlight issues at the federal level for the resident alien. Resident aliens generally are taxed in the same way as U.S. citizens, meaning worldwide income including all interest, dividends, wages, or other compensation for services, income from rental property or royalties, and any other types of income must be reported.

## Balancing Taxation in Multiple Jurisdictions

As noted above, U.S. citizens and tax residents under the definitions provided above are required to report worldwide income on an annual U.S. income tax return regardless of whether such income is also taxed in a foreign jurisdiction. A taxpayer must file for any year in which gross income is equal to or greater than the applicable exemption amount and standard deduction. In other words, all income should be reported, regardless of the source of that income.

Many countries have established tax treaties with the U.S. to allow foreign nationals living in the U.S. to potentially be taxed at a reduced rate, or to be exempt from foreign income tax on certain items of income received from U.S. sources. If a treaty does not apply to a certain type of income, or does not exist with the U.S., then a taxpayer must report and pay tax on the income in both countries. In this situation, the taxpayer generally pays the total amount of tax owed in the higher tax jurisdiction and receives a foreign tax credit in the resident country for taxes paid to the nonresident country.

Many foreign countries (other than the United States) do not continue to tax their citizens on worldwide income if they no longer meet certain physical pres-



ence tests in the foreign country and will only tax income that is sourced directly to the foreign country. So, once you meet the substantial presence test in the United States to trigger U.S. resident income tax, you will want to make sure you also understand how that will affect any potential taxation in other countries.

## Complications to Maintaining Foreign Assets: Foreign Account Tax Compliance Act (FATCA)

Understanding taxation in the U.S. relating to foreign income and assets for U.S. residents has become increasingly difficult. Since the international tax crackdown began in 2008, the Congress has implemented additional mechanisms to increase compliance reporting by U.S. resident taxpayers with foreign financial interests. In 2010, FATCA was signed into law, creating a burdensome set of requirements that foreign financial institutions must implement to identify all U.S. connected customers and report applicable income to the IRS each year. FATCA also expanded the complex foreign informational reporting requirements for U.S. resident individuals with foreign financial interests (the most common foreign informational tax reporting requirements are broadly outlined in the Appendix).

Foreign financial institutions have two choices: either report all holdings and transactions of their U.S. clients to the IRS each year, or be subject to a 30% withholding on all U.S. sourced payments. Among other consequences, FATCA is forcing these institutions to decide whether the business they receive from U.S. clients is worth the extremely high costs necessary to overhaul their internal systems to comply with the law. As a result, foreign financial institutions have begun to shun U.S. connected clients rather than comply. Significant numbers of foreign banks have stopped working with U.S. residents or curtailed the services that they provide to U.S. customers. Other foreign financial institutions are expected to restrict or eliminate U.S. relationships in the future due to FATCA. As a result, it is increasingly likely that, as a foreign national who meets the U.S. income tax residency tests, you may encounter difficulty in maintaining foreign accounts while living in the U.S.

# Structuring an Optimal Portfolio of Assets

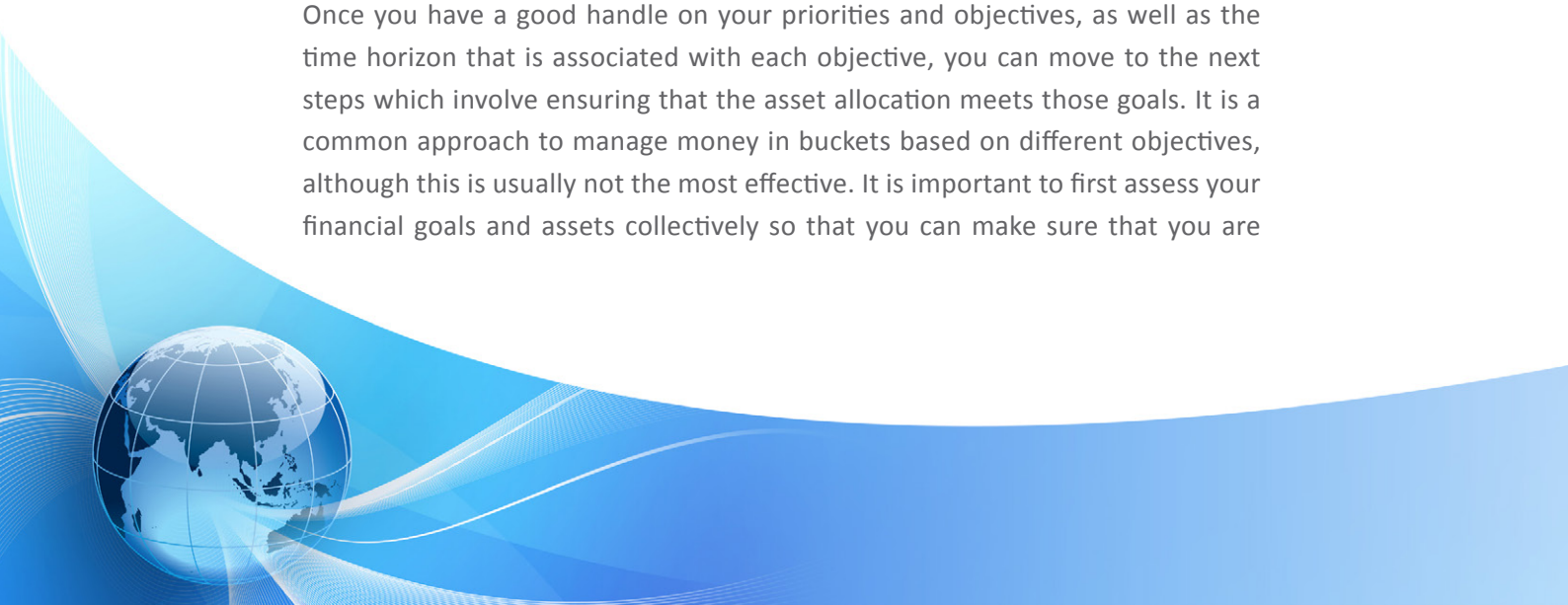
As a foreign national living in the United States, understanding the appropriate places to hold and invest your assets is just as important as knowing your tax compliance requirements. Understanding some basic planning principles can help avoid traps which could lead to unnecessary expenses and lower returns on invested assets.

An optimal portfolio considers priorities and objectives, time horizon, diversification, asset placement, tax efficiency, and currency exposure. A strict focus on only one area often results in a disjointed portfolio that lacks fundamental support of long-term needs. And, if your asset allocation correctly matches your time horizon, then the ever-present uncertainty in the markets over the short-term becomes less worrisome.

The first step in the development of an appropriate asset allocation is the identification of individual priorities and objectives. There are many significant milestones in one's life; career, children, grandchildren, parents, retirement. It is best to always have your goals, circumstances, and your attitude toward risk in mind. The key is to be flexible, aware and to plan. Individual priorities and objectives can be identified by asking some essential questions (but not limited to):

- What are your short-term and long-term goals?
- How will your current and future savings help achieve your goals?
- Do you have an accurate understanding of your consumption patterns?
- Would you rather spend less money now to have more money later?
- Do you have fixed liabilities that must be accounted for?
- Are you properly insured for the unexpected?
- Do you plan to permanently cease living in the United States at some point in the future?

Once you have a good handle on your priorities and objectives, as well as the time horizon that is associated with each objective, you can move to the next steps which involve ensuring that the asset allocation meets those goals. It is a common approach to manage money in buckets based on different objectives, although this is usually not the most effective. It is important to first assess your financial goals and assets collectively so that you can make sure that you are



appropriately accounting for the big picture. Not doing so might result in your assets having competing goals.

A simplified example can illustrate how this might happen. An individual has saved $100,000 in cash which is set aside to be used for a down payment on a future home purchase. This cash is not earning any interest. During the same time period, this individual is paying off $15,000 of credit card debt that carries an interest rate of 13.8%. Through regular monthly cash flow, a monthly payment of $1,000 is made to pay down the balance owed. In the 17 months that it would take to pay off the credit card debt, this individual would pay $1,563 in interest making the total outlay of cash $16,563. Instead of paying off the credit card debt with the cash saved for the home purchase and having $85,000 saved in cash, the individual has netted $83,437. By looking at the big picture an individual is able to allocate assets in a way that maximizes the net outcome most appropriately.

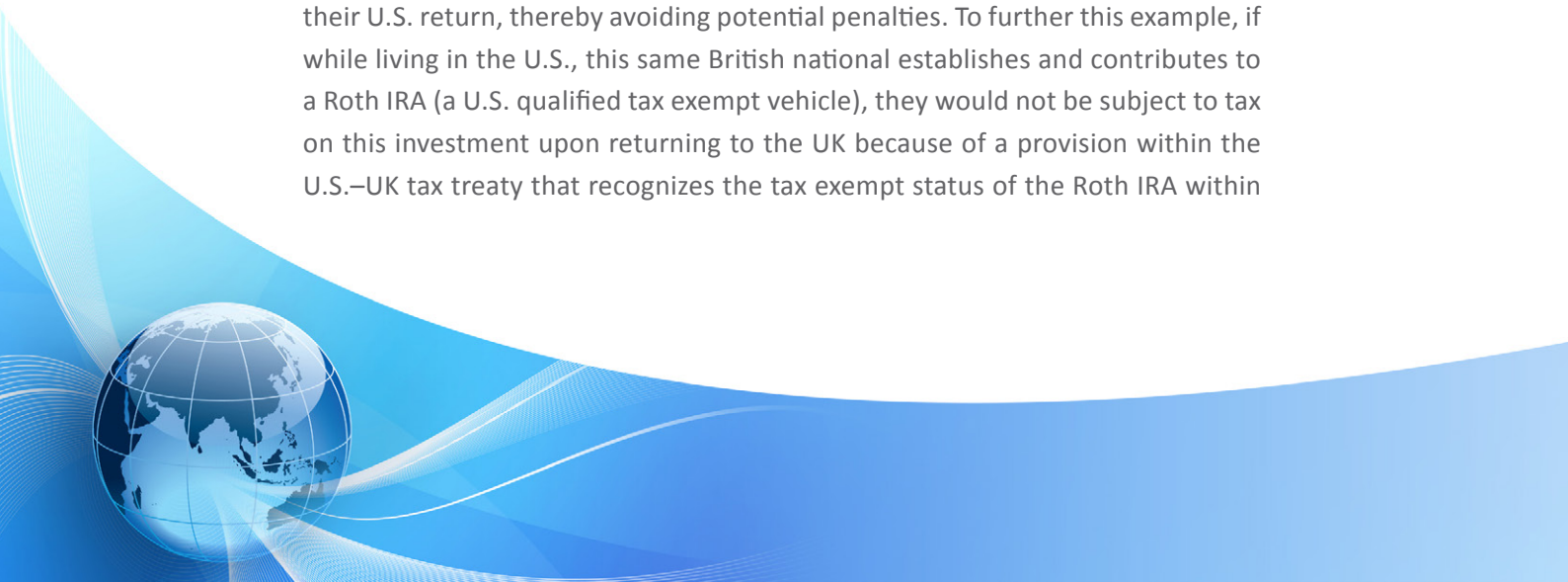
Regardless of where you hold the assets, a portfolio built on broad diversification provides the best opportunity for success in accomplishing defined objectives. This applies to diversification across asset classes and industry sectors as well as currency exposure. A globally diversified portfolio provides exposure into all sizes, styles, and types of companies as well as assets located throughout the world. Investing in a broad array of assets and sectors of the market helps mitigate the level of volatility within a portfolio and a disciplined rebalancing strategy helps an investor to separate emotions from the investment decision.

With this in mind, choosing specific investments to include in a portfolio should be done with an understanding of the potential large tax differences impacting the bottom line. Chances are that you may already have investment accounts established in your home country. We have stressed this before, but it is imperative that you either speak to knowledgeable professionals or do some research and planning before entering the U.S. Your already established portfolio investments may have potentially large U.S. tax consequences impacting the bottom line. For example, as a U.S. tax resident unless certain elections are made up front, any benefit of owning a mutual fund or an Exchange Traded Fund (ETF) that is registered in a foreign jurisdiction is quickly erased due to the punitive tax treatment of Passive Foreign Investment Companies (PFICs) in the U.S. (discussed in the Appendix). Owning a portfolio of similar securities through a U.S. institution could support the same long-term goals at a considerably less cost.

Since foreign nationals living in the U.S. need to make financial decisions with both tax regimes in mind, it is important to understand that many non-U.S. investment structures, including non-U.S. retirement accounts, are labeled as tax efficient or tax exempt in a foreign country but do not provide the same beneficial treatment for tax purposes in the U.S. For many non-U.S. tax favored investment structures, one must look-through and tax the investments held as though the structure does not exist. These structures also have foreign financial disclosure requirements which can be complex and costly. Therefore, if possible, it is almost always best to avoid incorporating these structures into your overall financial strategy as a U.S. tax resident. And, if you already have some of these plans in place prior to your arrival in the U.S., it is important that you understand the tax compliance requirements associated with them and mitigate any unfavorable tax consequences to any extent possible.

Likewise, it is important to be aware of how various U.S. tax advantaged plans will be recognized for tax purposes in the foreign country should you return to living at some point in the future. While some countries recognize the tax status of the U.S. retirement plan through the tax treaties, others do not. So, before employing a specific savings option, it is important to know how holding the account will be treated in both jurisdictions at different points in time. If you do not follow some of these plan rules properly, it can result in taxation or even loss of tax deferred status.

A specific example can illustrate how the tax consequences of certain investment vehicles can differ between countries. Suppose a British national moves to the U.S. for three years and has an established ISA that is recognized by the UK tax authorities as tax exempt. Since their intention is to return to the UK, they maintain the account in the UK, enter the U.S. and become a U.S. tax resident. While the ISA is tax exempt in the UK, the ISA becomes taxable in the U.S. because it is not recognized as a qualified pension plan for U.S. purposes. In this instance, planning upfront won't allow the individual to avoid taxes but it will allow them to ensure that they properly disclose the account and report the income on their U.S. return, thereby avoiding potential penalties. To further this example, if while living in the U.S., this same British national establishes and contributes to a Roth IRA (a U.S. qualified tax exempt vehicle), they would not be subject to tax on this investment upon returning to the UK because of a provision within the U.S.–UK tax treaty that recognizes the tax exempt status of the Roth IRA within



the UK. Again, planning accordingly with both jurisdictions in mind can prove to be extremely beneficial in developing a low cost tax efficient strategy.

So, how do you put all of the pieces together? While you may not be inclined to move your investable assets to the U.S. when it may not be your intention to remain here for more than a few years, there can be many benefits to doing just that when you fall under the U.S. tax system. For an individual that is taxed as a U.S. resident, a globally diversified tax efficient strategy is best accomplished from the U.S. A U.S. based investment account provides unparalleled access to more U.S. and non-U.S. companies than any other market in the world. In 2011, the U.S. markets (NASDAQ and NYSE) offered investment access to 4,988 companies. London offered investment access to 2,886 companies while Tokyo offered access to 2,291.[1] And, in addition to the more favorable tax consequences, securities held in a U.S. based portfolio generally incur lower commissions, transaction costs, and create simpler tax compliance requirements, all which boost net returns.

While investment accounts held in the U.S. are reported on statements in U.S. Dollars (USD), your true currency exposure is tied to the underlying assets that you own and where those assets derive their earnings. So, if a company is incorporated in the U.S. but derives much of its earnings in Europe, then your investment in that company will not be entirely exposed to the fluctuation of the USD. Similarly, if a company is incorporated in Europe and derives much of its earnings in the U.S., then your investment in that company will not entirely be exposed to changes in the Euro. Additionally, many non-U.S. companies that trade on a foreign exchange also trade on the U.S. stock exchanges in the form of American Depositary Receipts or American Depositary Shares (otherwise known as ADRs or ADSs). ADRs reduce the costs associated with owning securities directly on a foreign stock exchange.

ADRs are denominated in USD, with the underlying security held by a U.S. financial institution overseas. Each ADR is equal to a fixed ratio of shares related to the foreign stock it represents. The price of an ADR corresponds to the price of the foreign stock in its home market, adjusted to the ratio of the ADRs to foreign company shares. At any time, an investor has the right to obtain shares directly in the foreign stock itself by trading in the ADR shares. An ADR benefits from the same returns and currency exposure as owning the same security on the foreign

[1] World Federation of Exchanges, data as of December 31, 2011.

exchange. While it appears that returns are different between the foreign security and the ADR version of the same security, the currency fluctuation during that same time period accounts for the change in returns.

An example will help illustrate this point. Novartis, a Swiss company, trades in Switzerland on the SIX and also trades on the NYSE in New York. The below graph illustrates the change in returns on for shares owned in Switzerland and shares owned in the U.S. between December 2008 and December 2011. During the three year holding period, shares on the Swiss exchange returned -0.5% while shares trading on the NYSE returned 14.7%. During this same period of time, the Swiss Franc appreciated against the US Dollar by 15.1%. The difference in the rate of return offsets the change in currency.

## Comparison of an Investment in Novartis on SIX (CHF) and NYSE (USD)

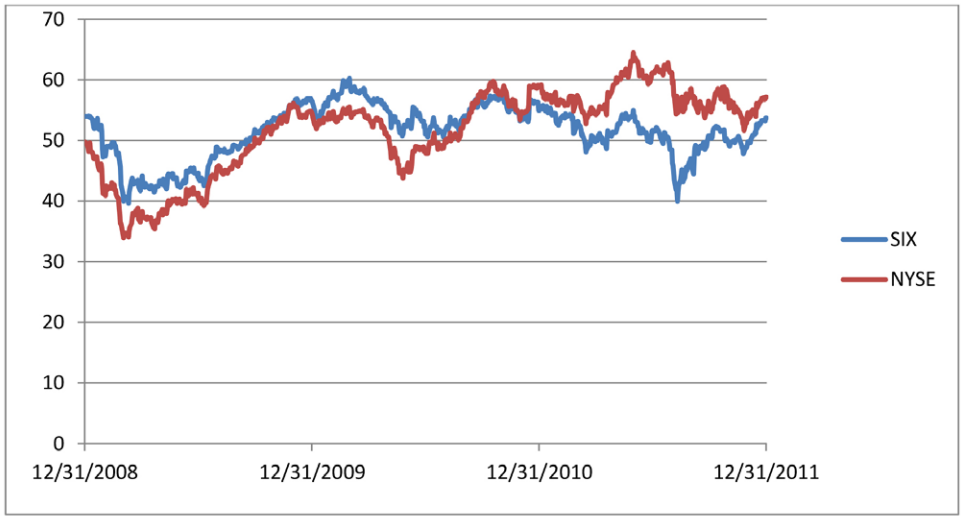
For the investor who does not wish to incorporate individual securities in their portfolio, low cost U.S. mutual funds and ETFs can accomplish asset allocation objectives. If, in the future, you are preparing to cease living in the U.S. then planning should be done to take into account foreign tax considerations on portfolio structure and investment assets. In the same way that foreign mutual funds and ETFs can trigger PFIC taxation in the U.S., it is also possible that including U.S. mutual funds and ETFs in your portfolio can create negative tax consequences in some foreign jurisdictions. As such, including mutual funds or ETFs that are recognized in both the U.S. and the foreign country can be a suitable alternative. Additionally, there will need to be an understanding of how tax is applied when income or capital is remitted to the country in which they are resident. How to repatriate assets is as important a consideration as managing wealth while living in the U.S.

# U.S. Implications of Owning U.S. or Foreign Real Estate

The implications of owning real estate as a U.S. tax resident, whether located in the United States or in a foreign country, is another area that deserves upfront understanding and planning consideration.

Many individuals who move to the United States will choose to maintain a residence in their home country. While living in the U.S., it is common for those individuals to rent out the foreign property. Once an individual meets the substantial presence test to qualify as a U.S. tax resident, any income derived from a foreign or domestic rental property will generally be subject to tax in the U.S. The individual will report gross rental income and will be able to offset that gross income by rental expenses incurred during the tax year. Common rental expenses include, but are not limited to, mortgage interest, real estate taxes, cleaning, repairs, painting, insurance, and management fees. Another common expense is depreciation expense, which allows the taxpayer to deduct a portion of the purchase price of a rental property each year over the specified life of the property.

U.S. resident aliens who own U.S. property as a primary or secondary residence without converting it to a rental property have similar tax benefits that are available to U.S. citizens and permanent residents. Under current legislation, real estate

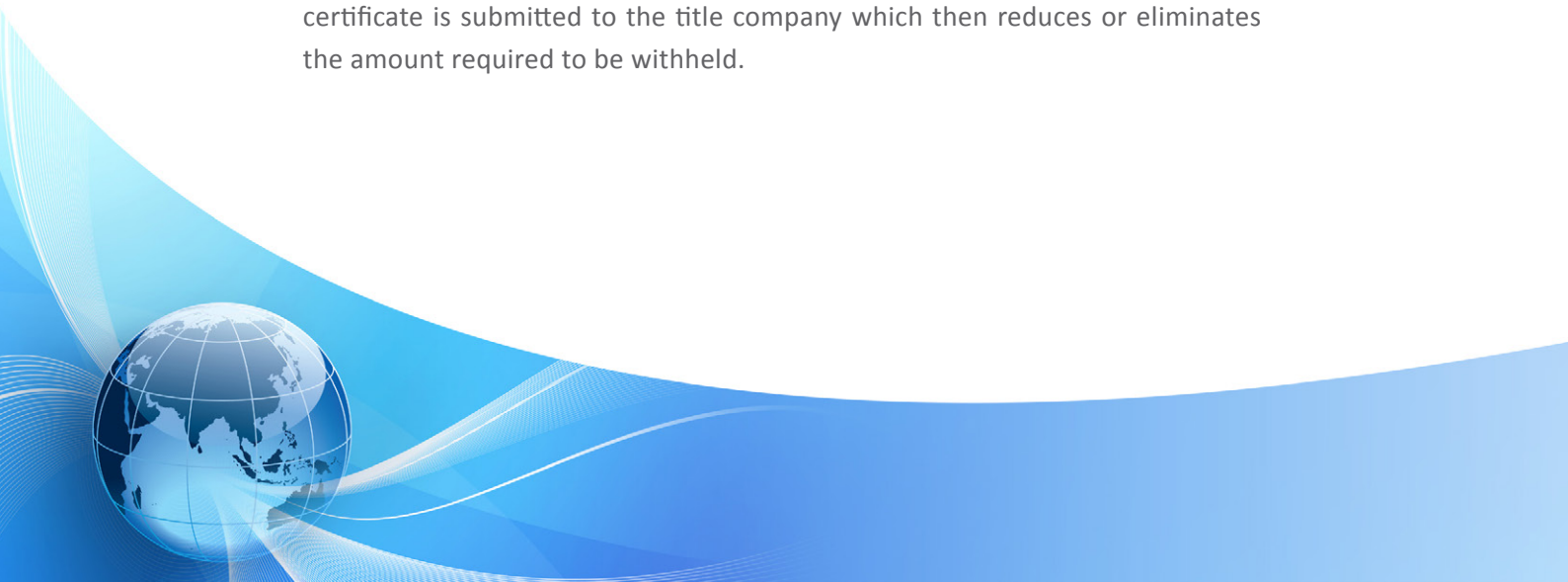



**Investment made from December 31, 2008 to December 31, 2011**

property taxes and mortgage interest paid on loans up to $1.0 million qualifies as itemized deductions to offset U.S. taxable income each year. If, under certain IRS definitions, the property qualifies as the taxpayer's primary home for at least 2 out of the last 5 years, each owner will receive a $250,000 gain exclusion on the sale before any U.S. income tax would apply.

If the individual decides to sell either their foreign property or their U.S. property while a U.S. tax resident, the gain realized on the sale of the property, as well as any depreciation recapture (if a rental property) is subject to U.S. taxes. Under current legislation, the portion of the gain related to depreciation recapture is taxed at 25%, and the rest of the non-excludable gain is taxed at 15%.

If you leave the U.S. at some point in the future, and no longer meet the tests associated with being a U.S. tax resident, then there will be different treatment and considerations to be aware of. For U.S. rental and investment properties, nonresidents are generally subject to a flat 30% tax on their gross rental income, with no deductions available for rental expenses incurred. However, an election can be made on their U.S. nonresident tax return to treat rental income as income effectively connected with a U.S. trade or business. As a result, the taxpayer is allowed to deduct rental expenses, and the net rental income is subject to the graduated rates applicable to U.S. tax residents. The election remains in effect until it is revoked. The Foreign Investment in Real Property Tax Act (FIRPTA) requires back up withholding of 10% on the sale of U.S. real property by a non-resident alien at the time of sale. If the taxpayer does not apply for a withholding certificate, the withholding is submitted to the IRS by the title company at the time of closing and will be applied to the gross sales price. The taxpayer will then need to file a U.S. nonresident income tax return after the calendar year has ended to receive any applicable refund. In order to avoid unnecessary withholding, a nonresident may file a Form 8288-B, which permits taxpayers to request a withholding certificate from the IRS, reducing or eliminating the withholding based on a claim that shows that the taxpayer's maximum tax liability is less than the 10% withholding. Upon approval from the IRS, the withholding certificate is submitted to the title company which then reduces or eliminates the amount required to be withheld.



## Other Noteworthy Planning Areas - Gifting, Estate, and Exit Tax

While this document does not go into detail, it is appropriate to mention a few additional planning items that individuals should be aware of once becoming a U.S. resident. It is possible that, while living in the U.S., you might decide to gift money to a spouse or family member, become a beneficiary of a U.S. estate, or choose to obtain a green card. If you seek to employ any of the following planning areas, it is important to take the time to consider the status of each individual and also assess the gifting and estate consequences in both potentially applicable jurisdictions. Somewhat different than income tax residency, for U.S. gift and estate purposes, residency is determined based on domicile.

Whether living in the U.S. or overseas, there are many couples who are connected to the U.S. in some way. This means that one spouse is considered a U.S. person while the other is either a dual citizen or nonresident of the U.S. It also applies to those individuals who might have a U.S. citizen in their immediate or distant families. An individual's tax status can impact gifting and estate strategies. For instance, in 2012, gifting money to a non-U.S. citizen spouse (including green card holders) is allowed up to $139,000 per year (an annual adjustment applied) without any gift tax being imposed. Also, one can gift up to $13,000 (in 2012) to individuals other than spouses each year, free of gift tax. With respect to estate tax for non-U.S. citizens, without proper planning with certain trusts, estate tax is assessed immediately on the entire taxable estate at a rate upwards of 35%.

If, at some point in the future, you decide to become a green card holder, it is important to be aware of the Exit Tax. This tax applies to certain U.S. citizens and "long-term residents" (defined as an individual who has held a green card in at least 8 out of the prior 15 years) who relinquish their U.S. green card and are considered "covered expatriates" under the definitions of IRC 877A.

A covered expatriate is required to calculate the gain on all of his or her assets as if those assets were sold on the day before expatriation, and pay an exit tax on the gain above a certain exclusion amount ($651,000 in 2012). The exit tax rules are extremely complex, and application heavily depends on each individual's facts. It is important to be aware that this tax regime exists, and it is best to have

an understanding at the outset of becoming a green card holder so that you have the best opportunity to plan accordingly.

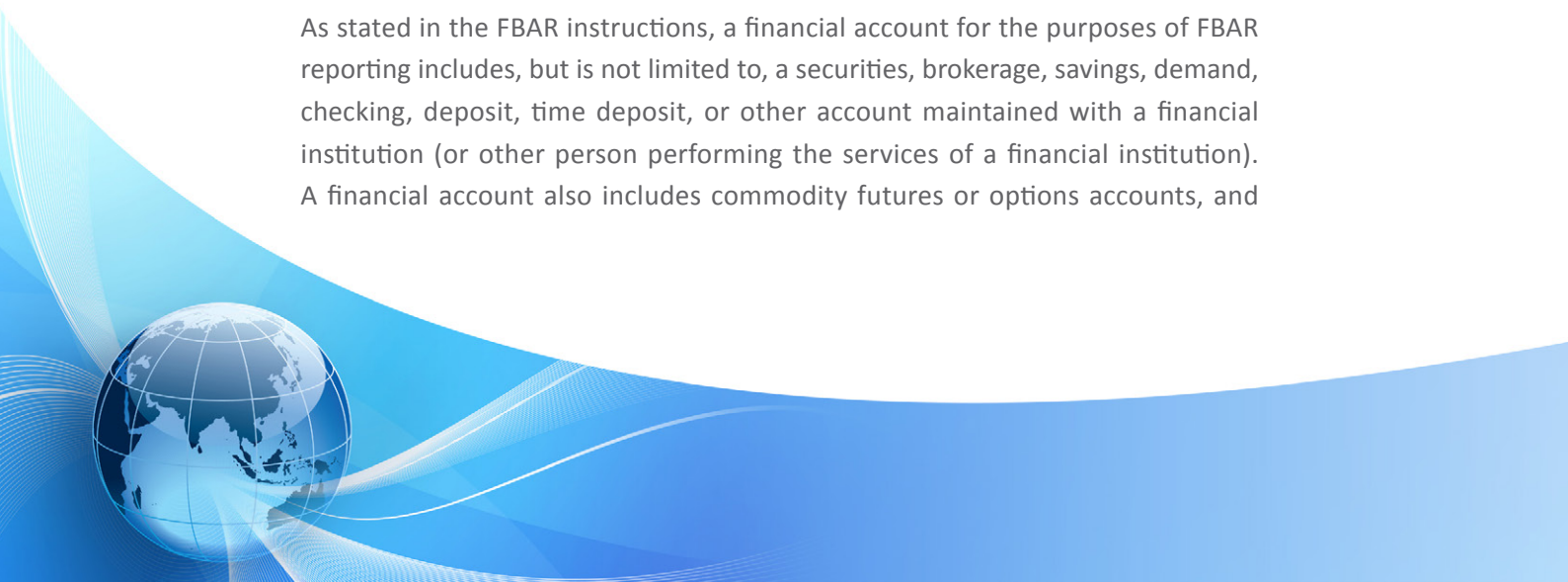
## Appendix: An Overview of Foreign Informational Reporting Requirements

There are a myriad of complex informational reporting requirements that U.S. tax residents must complete relating to their interest in foreign accounts and assets. While some of these forms are incorporated into the filing of an annual tax return, the FBAR and Form 3520, discussed below, have separate filing instructions from the tax return itself. Even though these forms are informational and do not result in additional tax, failing to file any of these forms in a given year can result in very large penalties that range anywhere from $10,000 to 50% of the maximum balance held in an account. A U.S. taxpayer that has any of these filing requirements should make certain they are satisfactorily meeting their obligations.

*Form TD F 90-22.1, Foreign Bank Account Report (FBAR)*

U.S. persons are required to file an FBAR if the person had a financial interest in, or signatory authority over, at least one financial account located outside the United States and the aggregate value of all foreign financial accounts exceeded $10,000 at any time during the reportable calendar year. A U.S. person is defined as a U.S. citizen, green card holder and persons meeting the Substantial Presence Test (generally, those who are present in the United States for the equivalent of 183 days or more when applying a three- year look-back test). If you qualify as a U.S. tax nonresident alien but elect to file jointly with a resident alien spouse, then the spouse who would otherwise be a nonresident for U.S. tax purposes is not required to report their foreign accounts on the FBAR form.

As stated in the FBAR instructions, a financial account for the purposes of FBAR reporting includes, but is not limited to, a securities, brokerage, savings, demand, checking, deposit, time deposit, or other account maintained with a financial institution (or other person performing the services of a financial institution). A financial account also includes commodity futures or options accounts, and



life insurance or annuity products with a cash surrender value. Additionally, it includes shares of a mutual fund or similarly pooled fund that is available to the general public with a regular net asset value determination and regular redemptions. Private equity funds and hedge funds fall outside of this definition.

*Form 8621, Return by a Shareholder of a Passive Foreign Investment Company or a Qualified Electing Fund*

Foreign registered mutual funds are generally not required to distribute annual income to shareholders as U.S. registered mutual funds are required to do. To level any investment income tax advantages between U.S. resident owners of foreign mutual funds and owners of U.S. mutual funds, Congress passed legislation containing special rules for "Passive Foreign Investment Companies" ("PFICs").

Two tests are used to determine whether a foreign corporation is a PFIC: (1) the income test and (2) the asset test. A foreign corporation is considered a PFIC if it passes either test. Under the income test, a foreign corporation is a PFIC if 75% or more of its gross income is passive income. Under the asset test, a foreign corporation is a PFIC if 50% or more of the average value of its assets produce (or could produce) passive income. Foreign mutual funds generally satisfy both of these tests. Unless a special election is made at the time of purchase, U.S. resident shareholders of PFICs are generally subject to the "excess distribution" regime. Excess distribution for a given tax year is determined by considering each PFIC separately. It includes all gains on dispositions of the PFIC stock, plus the portion of distributions from the PFIC that exceeds 125% of the average distributions for the prior three years. This income or gain is allocated evenly across the time the taxpayer owned the shares. The gain allocated to prior years is taxed at the maximum marginal rate in the U.S. during each year (regardless of the taxpayer's own marginal rate). Interest is computed on the prior year tax amounts from the due date of each year's income tax return to the date the tax is being paid. Capital losses realized on the disposition of PFIC shares are generally not recognized. Combined with the punitive nature of the PFIC tax regime, this makes it possible for the amount of tax due on PFIC income to exceed the amount of income earned!

In future years, reporting requirements for Form 8621 extend beyond those shareholders who received a distribution from the PFIC or recognized a gain on the disposition of PFIC shares during the year and require U.S. resident share-

holders to file an annual report for each year that they maintain PFIC positions. A disposition is any transaction or event that constitutes an actual or deemed transfer of property for any purpose of the Internal Revenue Code, including, but not limited to, a sale, exchange, gift, or transfer at death. Gains recognized on the disposition of PFIC shares are reported on a tax return on Form 8621, as opposed to Schedule D, because they are subject to a different taxation regime as noted above.

*Form 3520, Annual Return to Report Transactions and Receipt of Certain Foreign Gifts*

A U.S. person (and executors of estates of U.S. decedents) must file Form 3520 to report certain transactions relating to foreign trusts or receipt of certain large gifts or bequests from foreign sources. The IRS defines a U.S. person as a U.S. citizen or resident alien for income tax purposes, a domestic partnership or corporation, a U.S. estate or a domestic trust. In general, if a U.S. person forms, contributes to, owns or receives distributions from a foreign trust, there is a requirement to file this form. One important and overlooked thing to note here is that many non-U.S. pension plans are considered to be foreign trusts. Therefore, if you contributed to, or continue to contribute to, a foreign pension plan and become a U.S. tax resident, it is possible that you will have Form 3520 filing requirements related to that pension plan.

If the value of aggregate foreign gifts that you receive during any tax year exceeds a certain threshold, you must report each foreign gift to the IRS. A “foreign gift” is any amount you receive from a non-U.S. person that is either a gift or a bequest. A non-U.S. person is any person other than a U.S. tax resident, and includes a foreign estate.

For purposes of determining whether the receipt of a gift from a foreign person is reportable, different thresholds are applied for gifts received from individuals and estates than for gifts from partnerships and corporations. A U.S. person is required to report the receipt of gifts from a nonresident alien or foreign estate only if the total amount of gifts from that nonresident alien or foreign estate is more than $100,000 during the tax year. The receipt of gifts from foreign corporations and partnerships are reportable if the total amount of gifts from all such entities is more than $14,375 (for 2012).

*Form 8938, Statement of Specified Foreign Financial Assets*

Form 8938 is a new and additional reporting requirement, implemented as part of the increased effort and attention placed on international tax compliance through FATCA. It applies to all U.S. income tax residents who have specified foreign financial assets in excess of a threshold that varies from $50,000 to $600,000 depending on whether the taxpayer lives inside or outside the U.S. and whether they file a joint income tax return with their spouse. Unlike the FBAR, if a nonresident alien elects to file jointly with a resident alien spouse, both will be subject to the reporting requirements.

Specified foreign financial assets include foreign financial accounts and any foreign assets which are not held in an account. This includes any stock or security issued by a non-U.S. person, any financial instrument or contract held for investment that has an issuer or counterparty that is not a U.S. person, or any interest in a foreign entity, including foreign trusts and estates. An interest in a foreign pension is included as a reportable foreign asset. Foreign real estate is not a specified foreign financial asset unless it is held in an entity.

# About The Wolf Group, PC and Wolf Group Capital Advisors

Established in 1983, The Wolf Group, PC has become the premier CPA firm in the Washington, DC area specializing in international and expatriate tax planning and compliance. Wolf Group Capital Advisors is an affiliate of The Wolf Group, PC, created to supplement tax services with highly competent professional financial planning and investment management advice to expatriate individuals. Our unique ability to couple global tax expertise with solid investment principles enables us to provide our clients with holistic and simplified solutions to the complex issues unique to their circumstances.

The Wolf Group is a proud and active member of Nexia International. This network provides us with the resources and expertise to effectively and efficiently address the global tax and business needs of our clients. www.thewolfgroup.com

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GLOBAL WEALTH MANAGEMENT

# About Nexia International

Nexia International is a leading worldwide network of independent accounting and consulting firms, providing a comprehensive portfolio of assurance, tax and advisory services.

With more than 570 offices in over 100 countries, we have a substantial presence in the world's major financial and economic centres. We are strategically placed to serve the diverse international requirements of our clients, ranging from globally listed entities and international subsidiaries, to owner-managed businesses and high-net-worth individuals.

Experts from around the Nexia International network work together to provide cohesive, customised services to solve cross-border business issues and advise individuals on wealth creation and preservation.

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