


Global Mobility Solutions Practice Group

GGI North American Regional Conference

A Case Study

Drucker & Scaccetti

Tax As A Business Strategy®

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Case Study Facts

1. Mr. X, a U.S. citizen and resident, is considering emigrating to another country.

2. Mr. X is the sole shareholder of a U.S. corporation, an internet business with customers throughout the world.

3. Mr. X plans to continue to operate his business from his new country of residence.

Decisions Before Emigrating from U.S.

A. Retain U.S. citizenship
   1. Since the U.S. taxes its citizens and residents on their worldwide income, Mr. X will be subject to tax on the same basis as a taxpayer living in the U.S.
   2. Required to file an FBAR to report his foreign bank account in his new country of residence
   3. Subject to income tax in country of residence; may be able to reduce U.S. Tax by foreign tax credit
   4. Can exclude approximately $100,000 of gross earned income each year from U.S. taxation (§911)

Decisions Before Emigrating from U.S.

B. Expatriation (§877A)

1. A citizen or resident can only avoid U.S. taxation and become an expatriate upon the renunciation of citizenship or becoming a non-resident alien. He must eliminate all economic contact with the U.S. that will recreate tax residency or domicile.
2. Citizens who relinquish U.S. citizenship, or residents who relinquish their residency, are considered “covered expatriates” if one of the following tests are met:
   a) The individual’s average annual net income tax for the five years ending before expatriation exceeds an inflation adjusted amount of $161,000 for 2016.

Decisions Before Emigrating from U.S.

b) The individual's net worth as of the expatriation date is $2,000,000 or more, or
c) Individual fails to certify, under penalty of perjury, that he has met the requirements of the U.S. tax code for the five preceding years.
d) Any individual who meets one of these requirements will be subject to an exit tax. An expatriate who is not a covered expatriate is not subject to an exit tax.

Decisions Before Emigrating from U.S.

3. A covered expatriate is subject to mark to market rules under which all of their property is treated as sold on the day before the expatriation date for its fair market value, and the covered expatriate is subject to tax on the gain that exceeds $693,000 in 2016. In general, the gain will be treated as a sale of capital gain property unless it is certain business assets such as inventory, which is taxed as ordinary income.
   a) An election is available to defer the tax (§877A(b)) for certain deferred compensation items.
   b) Income from non-grantor trusts is not taxed upon expatriation, but is subject to a tax when the amounts are distributed (§877A(d) & 877A(f)).

Decisions Before Emigrating from U.S.

C. A transfer tax imposed on U.S. citizens and residents who receive gifts and bequests from expatriates.

  1. For covered gifts or bequests received after June 16, 2008, a special transfer tax (§2801) is imposed on any U.S. citizen or resident who received any gift or bequest from a covered expatriate, The tax rate is the highest gift tax rate in existence at the time of gift or bequest. For 2016, that rate is 40%.

Decisions Before Emigrating from U.S.

2. The tax applies to any covered gifts or bequests with a value in excess of the annual exclusion amount in effect for the gift tax purposes in the year of transfer ($14,000 in 2016). §2801(c).
   a) Covered gift or bequest means:
      i. Any property acquired by gift directly or indirectly from an individual who, at the time of the gift, is a covered expatriate, and
      ii. Any property acquired directly or indirectly by reason of the death of an individual who immediately before his death was a covered expatriate (§2801(e)(1)).

Decisions Before Emigrating from U.S.

b) Where a gift tax or bequest is made to a domestic trust, the §2801 tax applies in the same way as if the trust was an individual and, therefore, the trust pays the tax

c) If the gift or bequest is made to a foreign trust, the §2801 tax applies to any distribution attributable to the gift or bequest (whether made from corpus or income) from the trust to a U.S. citizen or resident.

U.S. Corporate Tax Issues

A. Retain U.S. corporation
   1. Taxed on worldwide income
B. Formation of foreign corporation and transfer of assets and liabilities.
   1. Since the stock of the U.S. corporation will be marked to market, the shareholder’s basis in the stock will be stepped up. Therefore, the corporation can be liquidated with no gain and the shareholder can contribute its assets to a newly formed foreign corporation.
   2. Must plan to avoid taxation under §367(a), transfers of property from the United States and §7874(a), tax on inversion gain of expatriated entities (corporate inversions).

Q&A

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