United States: Smooth Move: US Tax Tips Every Top Executive Should Know Before Moving To The United States

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If you are a foreign executive moving to the United States for work, not only do you have to consider practical concerns like moving your family and finding a new residence, but you also need guidance as to any US tax implications stemming from the move. One of the first tasks your US tax advisor should tackle will be to determine whether you will be a tax resident for US income tax purposes or transfer (*i.e.*, gift, estate and generation-skipping transfer) tax purposes based upon the amount of time you will spend in the United States.

There are different tests for tax residency for US income tax purposes and transfer tax purposes.

US Income Tax

A US income tax resident is subject to US income tax on worldwide income, which is often surprising for an executive moving to the United States from a different country. A green card holder is automatically a US tax resident when he enters the United States with the green card when he has received his green card abroad.

An individual who is neither a citizen nor a green card holder of the United States is treated as a resident of the United States for US income tax purposes if such person meets the "substantial presence test." The substantial presence test uses a weighted formula based on the number of days an individual has spent in the United States during the current calendar year and two preceding calendar years. The substantial presence test is met if an individual spends at least 31 days in the United States during the current calendar year and, based on the weighted average, is deemed to have spent 183 days or more in the United States during the current calendar year. In computing the weighted average, all of the days of US presence in the current calendar year are counted, one-third (1/3) of the days of US presence in the preceding year are counted, and one-sixth (1/6) of the days of US presence in the second preceding year are counted, and the three amounts are aggregated.

Certain exceptions to the substantial presence test may be relevant, such as the closer connection exception, which may apply if the individual spends less than 183 days in the United States in the current year but has met the substantial presence test for the current year based upon the weighted formula. To claim the closer connection exception, an individual must show that she had a "closer connection" to a foreign country in which such person also maintained a "tax home" for the entirety of the year by filing IRS Form 8840. The residency "tie-breaker rules" of an income tax treaty if one exists between the United States and the individual's home country may also be helpful. A treaty-based position taken by filing IRS Form 8833 only applies, however, for purposes of determining an individual's US tax liability and not with respect to determining whether such person has reporting obligations in the United States (*e.g.*, with regard to reporting foreign bank accounts and determining whether a foreign company is a "controlled foreign corporation", discussed below).

The "tie-breaker rules" of many income tax treaties with the United States commonly provide that if an individual is a "resident," as that term is defined in the treaty, of both the United States and the treaty partner country, preference is given to the country where the individual has a permanent home available to him, or if one is available in both jurisdictions, then such person is considered to be a resident in the place where his personal and economic relations are closer ("center of vital interests"). If no determination can be made based upon an individual's center of vital interests, residence is usually determined by an individual's habitual abode in a real and meaningful sense.

US Transfer Tax

While there is a bright-line test for US income tax residency, for US transfer tax purposes, the determination of residency is a little more complicated. Residency in the US transfer tax context means domicile. Under the US rules, domicile is physical presence with the subjective intent to remain indefinitely. The subjective intent of the prospective taxpayer is measured by a series of objective factors.

While not exhaustive, significant weight has been given to the following factors, any combination of which has been used in favor of, and at times against, a US domicile:

- Family immigration history;
- Type of visa and duration held (including obtaining a social security number);
- Number, location and relative importance of business activities and interests;
- Residential properties in terms of value, location, size, how the property is maintained (meaning as a permanent residence versus vacation property), and personalty kept at each location;
- Location and significance of sources of income;
- Location and significance of investments;
- Location and registration of cars and drivers' licenses;
- Location of personal banking relationships;
- Statements on personal, official, legal or financial documents;
- Motivation for being in the United States;
- Travel and duration of stays in the United States;

- Location of family and friends;
- Community affairs and group affiliations;
- Government-related benefits;
- Where one is registered to vote; and
- Location of physicians.

It would be possible for a non-resident alien to move to the United States and establish domicile quickly if she did not have a specific intent to leave the United States. A green card is presumptive evidence of US domicile, but this presumption may be rebutted.

Objectives

Before the foreign executive moves to the United States, his US tax advisor should analyze whether he (or his family) will become a tax resident for US income tax purposes and for US transfer tax purposes. Below is a checklist of considerations for a wealthy foreign executive to discuss with her tax advisor before moving to the United States:

1. Consider making a gift to a trust to shield assets from US estate tax to hedge against the possibility that the foreign executive may die while a domiciliary of the United States. The exemption against US estate and gift tax is USD5,430,000 for US citizens and domiciliaries in 2015, indexed for inflation. The exemption is USD10,860,000 for a married US domiciled or citizen couple. High net worth individuals with assets in excess of this amount should consider making a gift to a "drop-off" trust for their family before they become US domiciliaries. Ideally, the person funding the trust should not be a beneficiary of the trust, and he must have limited control over the trust.
2. Make gifts to family members before becoming US domiciled. If the executive intends to make outright gifts to family members of assets that are not considered US situs for US gift tax purposes (*i.e.*, assets other than tangible or real property located in the United States), she should make the gifts before becoming a US domiciliary.
3. Step-up the basis of assets to fair market value. Foreign executives should consult their US tax advisor as to how to step-up the basis for US tax purposes of assets that might be sold from historic cost basis to fair market value before becoming a US taxpayer.
4. Review investments to harvest gain and see if they are appropriate and tax-efficient for US taxpayers. Foreign executives should consider selling their interests in passive foreign investment companies ("PFICs") unless certain US tax elections are available. A foreign corporation is a PFIC if 75 percent or more of its income is passive in nature or 50 percent or more of its assets are held for the production of passive income. The PFIC regime applies regardless of the percentage ownership of the US shareholder, and there is a back tax and an interest charge on dispositions of the stock and certain "excess distributions." Capital gains tax treatment is also lost on the sale, and the PFIC regime is extremely punitive when the back tax and interest charge are aggregated. Most foreign mutual funds are PFICs.
5. Review ownership interests in offshore companies to see if US tax on income of these companies may be deferred offshore. Certain foreign corporations, known as "controlled foreign corporations," will have a deemed flowthrough of passive income to US shareholders who own at least 10 percent of voting power of the corporation's stock ("US

Shareholders"). A foreign corporation is a CFC if more than 50 percent of the foreign corporation is owned by vote or value by US Shareholders.

6. Determine whether dividends from a foreign company which the foreign executive will receive once a US taxpayer will be qualified dividend income for US income tax purposes, and restructure the holdings if possible to ensure qualified dividend status. Also, if the foreign executive is moving from a lower tax jurisdiction, consider accelerating receipt of any dividends prior to the move if possible.
7. Review foreign deferred compensation and other retirement plans as well as any applicable income tax treaties to see if they will provide deferral from US income tax.
8. Review the intended activities of the foreign executive in the United States to make sure that these activities will not subject a foreign employer to US income tax.
9. Determine whether the foreign executive and her spouse have community property prior to the move and sever the community property if necessary.
10. Create a plan to maintain flexibility in the pre-residency planning if the foreign executive is only moving to the United States for a potentially discrete period of time.

Below are several other considerations for the foreign executive to discuss with his US tax advisor as well:

1. *Time the arrival date.*If the foreign executive arrives in the second half of the calendar year, she may not become a US taxpayer under the substantial presence test until the following year.
2. *Understand US reporting requirements.*Once the foreign executive becomes a US taxpayer, in addition to being subject to US income tax on worldwide income, he will have to disclose his worldwide assets due to extensive US reporting requirements of US taxpayers with foreign assets. It is important that the foreign executive understand the scope of this web of reporting before becoming subject to it.
3. As discussed above, a*pre-residency plan should be flexible*to allow the foreign executive to leave the United States without triggering further US tax consequences. The client and her US tax advisor should have an exit plan in place to dismantle the structure shortly before or after the client leaves if necessary.

In summary, there are any number of issues for a foreign executive to consider when moving to the United States in addition to all of the practical minutiae stemming from a relocation, but he needs to discuss US tax planning with his US tax advisor well in advance of the actual move.

The content of this article is intended to provide a general guide to the subject matter. Specialist advice should be sought about your specific circumstances.