

Tax planning opportunities for US taxpayers post-Emergency Budget

No further information has emerged about the scope or timescale of the review of the taxation of non-domiciliaries since we issued our Budget report a few weeks ago. However, tax planning opportunities still exist based upon the rules that have been in effect since 6 April 2008.

Capital Gains

The rise in capital gains tax (CGT) from 18% to 28% for higher rate UK taxpayers, in terms of the interaction with US taxes, is not such bad news. Although there is already a margin between US tax on long-term gains (15%) and UK CGT, US tax rates are also expected to rise in 2011. The actual US rate for long-term gains could be as high as 20% or even 25%, which would maintain a similar difference.

If you are US citizen who is a remittance basis taxpayer in the UK, then it may be sensible to realise gains pre December 31 rather than wait until January 2011 - more on this toward the end of 2010 when we know where rates will be.

Remember that for property sales it is the completion date that is important for US tax purposes, whereas in the UK exchange is the key date.

For clients reporting worldwide income in the UK, the UK tax is likely to be higher on long-term gains (assets held more than 12 months) and lower on short-term gains (assets held 12 months or less). This can result in a "smoothing"

in the overall tax rate between the US and UK and may well give planning opportunities. These can be enhanced between husband and wife if one or both are not higher rate taxpayers.

Taxes generally - optimise your global tax

We still do not know where US tax rates will be next year but under President Obama's Green book proposals, published in May 2009 by the Treasury, they could be increased to 39.6%.

The overall planning for a US taxpayer living outside the US is to try to lower their foreign tax rate as close as possible to the US tax rate, remembering that you will always pay the higher of the two taxes. The 50% tax rate has received a lot of publicity in the UK, and for an American, pension contributions can be effective, even when only relieved at 20%, in bringing the overall UK rate down and therefore closer to US rates.

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For example, a 50% taxpayer making a contribution of £60,000, will get a minimum of £20,000 relieved at the highest rate, with the remainder relieved at 20%. This would give effective tax relief overall at 30%.

Anyone whose income is likely to be between £100,000 and £112,950

(or just over) for 2010/11, is advised to consider enhancing their pension payments to a UK approved pension or making a charitable contribution to a UK registered charity. A dual qualified UK/US charity is even better! By doing so more of the personal allowance (£6,475) can be preserved, saving tax at a rate of 60%!

Although the top rate of tax on income up to £150,000 is only 40%, because of the loss of allowance between £100,000 and £112,950 of income, the effective tax rate of income in that band is 60%. The benefit of assessing this before year-end and taking steps to reduce taxable income can be considerable.

Be careful about shifting income into your husband or wife's name if you are not UK domiciled or if you are not both US citizens. In such situations planning should always be checked with an adviser.

Investment issues

Don't forget that most non-UK funds (such as US mutual funds) are subject to UK income tax on disposal and not CGT. The definition of an offshore fund changed in the UK in 2009 but has not helped the position particularly and our current view is that the income tax rules would apply to exchange traded funds as well

- Repayment of a UK mortgage can result in a currency gain for US tax purposes, where the \$ has strengthened against the £ during the period of the loan. This gain is taxed as ordinary income.
- Neither currency losses on mortgages (if the \$ weakens during the life of the mortgage) nor losses on main residences are allowable for US (or UK) tax purposes. Both are regarded as personal assets;
- Investing in UK funds will generally be tax disadvantageous for US tax purposes and increase the complexity of filing a US return.
- Think carefully about the currency you invest in - both the US and UK are interested in profits realised on "foreign" currency regardless of whether you regard it as an investment or not. There is planning available that might reduce the impact of currency gain reporting in the UK.

Attention Green card holders!

As well as US citizens, people who have had US Green Cards can be subject to the expatriation rules in the US if they are regarded as "long term residents". Regardless of where they are living, a Green Card holder who filed as a US resident in at least 8 taxable years and then relinquishes the Green Card at a later date will be affected.

Since June 2008, these rules can result in a deemed disposal of all assets as of the day before the date of expatriation, with US tax to pay on a "mark to market"

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basis. Clients may be less aware of the fact that certain unexpected events can trigger expatriation such as:

- Filing a treaty based tax return (form 1040NR);
- The date of filing Department of Homeland Security Form I-407 with a US consular or immigration officer;
- The date of removal from the US under the Immigration and Nationality Act

We are aware that some Green Card holders who have lived for a long time outside the US are having their Green Card status challenged at US immigration. With summer holidays approaching we want to alert clients that if this results in the removal of a Green Card there could well be tax implications.

Please ensure that you are meeting the terms of your Green Card and if in any doubt, consult with an immigration lawyer. We would be happy to put you in touch with immigration specialists if need be.

Early warning for December 2010

Those US taxpayers already claiming foreign tax credits on the "paid" basis and wishing to take a credit on their 2010 US return for UK tax for the 2009/10 tax year, must ensure that the balancing payment is made by 31 December 2010. The best way to do this is by cheque. If you will want your UK tax return before Christmas in time to make this payment we must have the completed UK checklist back by Monday 1 November. This is because the run up to the end of the calendar year is particularly busy.