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TAXATION OF INTERNATIONAL OPERATION OF U.S. RESIDENTS

a. ***Overview***

In order to tax nonresident aliens, the United States uses two different taxing theories which are known as the 'Worldwide Taxation regime' and the 'Territorial regime'. In a Worldwide Taxation Regime, residents are taxed on their worldwide income. To eliminate the same income being taxed by two jurisdictions, credit is taken on the resident jurisdiction tax return for taxes paid to other tax jurisdictions. In a Territorial Regime country, residents are not subject to taxes on income earned elsewhere than their resident jurisdiction. Taxpayers will allocate the total income among various jurisdictions and report to the appropriate one; credits are not taken.

b. ***Foreign Tax Credit***

A Foreign Tax Credit (FTC) is a form of relief from double taxation on foreign earned income. An FTC only applies to income taxes; foreign excise taxes, sales taxes, transfer taxes, and property taxes are not

creditable. An FTC is subject to a significant limitation. The annual credit cannot exceed a specific percentage of the precredit U.S. tax for the year. This percentage is the taxpayer's foreign source income divided by taxable income.

c. GILTI

GILTI, or Global Intangible Low Taxed Income, is the attempt by the United States government to tax value held offshore which they deem to be above a normal rate of return. It was originally introduced in the 2017 Tax Cuts and Jobs Act. Although the GILTI formula is complicated, the amount tax is roughly equal to the gross income of the foreign corporation minus the 'deemed tangible income return'. The deemed tangible income return is basically the depreciable assets of the business minus any interest expense attributable to the foreign corporation. If the aggregate earnings in a controlled foreign corporation exceed what Congress thinks is a 'normal' profit margin, then that amount is taxed by GILTI in the United States. The takeaway for the taxpayer is that when they are a United States shareholder and they own over 50 percent of the voting power or value in a foreign corporation, the taxpayer needs to be aware that there are compliance issues due to GILTI.

d. ***PFIC***

A Passive Foreign Investment Company (PFIC) is a corporation located abroad that meets one of two conditions: – At least 75% of their income is passive, – At least 50% of the company's assets are investment. United States investors that own shares of a PFIC must file a Form 8621, Information Return by a Shareholder of a Passive Foreign Investment Company or Qualified Electing Fund, with the IRS. In 1986, Congress

wanted to close tax loopholes that allowed US taxpayers to shelter offshore investments from taxation. Congress not only wanted to bring such investments under US taxation, but they also wanted to discourage taxpayers from this practice. Sections 1291 through 1298 of the US Income Tax Code define PFICs.

Form 8621 is intricate; it is estimated to take around 40 hours to fill out. Generally, investors turn to tax professionals for assistance and guidance on PFICs & Form 8621.

e. CFC

A Controlled Foreign Corporation (CFC) is a corporate entity that is registered or conducts business in jurisdictions or countries different than the residence of their controlling owners. Under IRC § 957, the term controlled foreign corporation means any foreign corporation if more than 50 percent of the total combined voting power of all classes of stock or the total value of the stock of such corporation is owned or considered as owned by United States shareholders. United States shareholders means a United States person who owns 10 percent or more of the total combined voting power (or value) of all classes of stock. CFCs prove to be advantageous when the cost for setting up a business, partnerships, or foreign branches is less than the tax implication costs.

Conclusion

This alert is a very brief discussion of international tax requirements of US persons with international operations and is not all inclusive. There additional tax requirements for US persons with foreign trusts, partnerships and other types of arrangements that may apply.

We recommend that you consult with an international tax attorney to determine the applicable requirements and obligations.

Should you need additional information it will be our pleasure to assist you

Sincerely,

Ruben Flores, Attorney & CPA

As requirement of the United States Treasury Regulations, you should be conscious of the fact that this notice has not been written to be used and it should not be used by the recipient to prevent penalties that could be imposed by U.S. Federal Law.