

Question 1

Part 1 - The tax effects of filing to have SFS as a disregarded entity are as follows:

- the entity will be treated as a foreign branch and as such its income or losses will be included in the taxable income of Oklacorp.
- the losses incurred due to the start-up nature of the business will be available to be used to reduce the taxable profits of Oklacorp.

Part 2 - the losses of \$3m (2013) and \$400,000 (2014) will be included in the taxable profits of Oklacorp and the impact will be losses will serve to reduce the taxable profits of Oklacorp and thereby reducing the federal tax liability.

Part 3 - the proposal to file SFS as a corporation from 1 January 2015, will be that the company will be subject to Branch loss recapture. The branch loss recapture regime is aimed to avoid a situation where a loss making branch is restructured as a corporation just before it becomes profitable. The reason for the branch changing its entity status is primarily to avoid paying tax when it becomes profitable. Also as foreign subsidiary, it will not be subject to US until the income is repatriated in the form of dividend or otherwise. Hence, congress enacted the anti-avoidance rule whereby the losses of \$3m (2013) and \$400,000 (2014) will be clawed back and treated as taxable income. As such, \$3,400,000 will be subject to federal tax when SFS is entity is recharacterised.

Part 4 - If SFS is profitable in 2015 (as a disregarded entity - its profits will be included in the taxable profits of Oklacorp.

If SFS is profitable in 2015 as a corporation, its income will not be taxable in the US but only when the income is repatriated (under the deferral rule) will any tax liability arise.

Part 5 - Code s 951(a) if a foreign corporation is controlled for a continuous period of 30 days or more by a United state citizen or corporation, this will fall into the regime of controlled foreign corporation (CFC) and as such, the US corporation must include their pro rata share of the gross income of the foreign entity in their taxable income for the year. The Subpart F income will be gross income based on a pro rata basis for the taxable year.

Question 2

Advise as to whether X Corp a foreign entity based in Xanthera - Permanent Establishment Issues

Part 1 - In accordance with the Article 5 (Permanent Establishment) PE means having a fixed place of business through which the business of an enterprise is wholly or partly carried on. Based on the given facts - there is no information as to whether there is a treaty agreement between X Corp and United States. The transaction between X corp and D corp (based on the facts given D Corp is an independent agent as the entity does have several distributors within the US market. Hence, the transaction between the entities will be deemed to a regular distributor agreement and Xcorp should not have any exposure to US taxes. The rationale being that D Corp is acting an independent agent and is not related to X corp.

Part 2 - The situation changes whereby X Corp appoints D Corp and its agent to sell the widgets to retailers in the Unites States and pay a commission for this transaction. The main question is whether this agreement will trigger a permanent establishment (PE) for Xcorp. Based on the facts D cORP will handle all solicitations and negotiations with the US retailers. In accordance with the provisions of Art 5 (6) - an enterprise will not have a PE merely because an agent or an independent agent provided that such persons were acting in the ordinary course of their business as independent agents. Additional information will be required in order to determine the exact and detailed nature of the transaction between Xcopr AND dcORP. bASED ON THE GIVEN FACTS d CORP DOES HAVE SEVERAL COMPANIES THAT IT PROVIDES AGENT TPE SERVICES. The commission that it is paid - is this a reasonable for the nature of work carries out.

Part 3 - Based on the provisions of Art 5 (4) (a) and (b)- X corp does have a warehouse for storage - this warehouse in itself does not give PE to Xcorp. "The maintenance of a stock of goods ----- solely for for display

Part 4 - based on the facts that sales contracts are made

Part 5 - The interest income will be US sourced and as such will be subject to withholding of 30% and in the absence of a treaty agreement between UNITED STATES AND xanthera - there will be no reduction in the withholding rates.

Question 3

Part 1

Part a - The debenture purchased by LuxInvest on 1 MAY 2015 is part of portfolio. In this regard, the interest earned by LuxInvest will be portfolio interest and there will be exempt from any withholding tax.

Part b - LuxInvest investment in Calcorp, which represents 20% of the Calcorp voting common stock will be treated as being effectively connected to a US trade as the investment is fairly significant in that it exceeds 10% of the voting stock. Also although Calcorp has not paid any dividends the net profits generated by Calcorp will be US taxable income on LuxInvest as the nature of this income was due to trade and business effectively connected with the US.

On 1 May 2015 - The additional investment of \$10m corporate bonds with interest 6% in Calcorp. This will yield interest of \$350,000 ($6\% \text{ @ } \$10,000,000 \text{ divided by } 12 \text{ months multiplied by } 7 \text{ months}$). This will be subject to withholding tax but given that there is a treaty agreement in place between United States and Luxembourg, this could potentially be reduced to 0%

Part c - 1 July 2015 - LuxInvest investment of \$20m which represents 0.05% of the shareholding in Amalgam is not substantial and as such the dividend received for 2015 ($\$5 \text{ @ } 200,000 \text{ shares @ } 2$) = \$2,000,000 will be subject to withholding tax of approximately 15% but given that there is a treaty agreement in place between United States and Luxembourg this withholding tax rate will be reduced to possibly 5%.

The dividend calculation is based on the fact that the dividend is paid quarterly and given that LuxInvest had owned the shares for 6 months (that is from 1 July 2015 to the end of the calendar year).

Part d - 1 October 2015 - LuxInvest sold 1m shares of shares of ShopCTR Inc. Under CODE SEC 897 (C)(1) - the term United States real property interest means an interest in real property located in the US and under (code s897 (2) (A) the fair market value of the US real property interest equals or exceeds 50 percent of the the fair market value of its US. The gain generated on disposal \$11m (disposal proceeds less \$5m) will be subject to withholding tax of 30%. The treaty agreement between United States and Luxembourg will not reduce the withholding tax applied.

Part 2

Code s 951(a) if a foreign corporation is controlled for a continuous period of 30 days or more by a United state citizen or corporation, this will fall into the regime of controlled foreign corporation (CFC) and as such, the US corporation must include their pro rata share of the gross income of the foreign entity in their taxable income for the year. The Subpart F income will be gross income based on a pro rata basis for the taxable year.

Part a. - Based on the facts - the wholly owned Romanian manufacturing entity meets the definition of a CFC, especially where the refrigerators manufactured are in Romanian and sold in Romanian and elsewhere in European. This particular entity's income will not be a Subpart F income and as such there will be no inclusion of the gross income in USP taxable return. The Romanian income will not be subject to US tax until the income is repatriated, the Romanian is actively trading and was not created in order to avoid taxes.

Part b. - Based on the given facts and the definition of what would constitute as subpart F income - the Romanian retailing subsidiary is a CFC but it will not be a Subpart F income and as such there will be no inclusion of the gross income in USP taxable return. The Romanian income will not be subject to US tax until the income is repatriated.

Part c - Based on the facts the Estonian retailing subsidiary will not fall into the Subpart F income regime this particular entity's income will not be a Subpart F income and as such there will be no inclusion of the gross income in USP taxable return.

Part d - The Estonian wholesaling subsidiary is also a CFC but is also a Subpart F income as the the refrigerators are not manufactured or consumed in Romanian or Estonian and as such the gross income will be subject to Subpart F and the gross income will be included in the taxable income of USP.

Part e- The same as in part d - will be Subpart F income and therefore included in USP taxable income.

Part F - Based on the given facts, the Estonian subsidiary is a CFC - under the foreign personal holding company (Code 956 (c)- the gross income of this corporation consists of dividends, interest, royalties and annuities and rents. Based on the definition as above this entity is a CFC and the income will be a Subpart F income and will be included in USP taxable income.

Question 5

Advise on the the disposal of stock on United States Property Holding Corporation by Gaspar ___

The facts provided can be summarised as follows;-

- 1.) Gaspar is not a citizen or resident of the United States (US)
- 2.) His investment in the US Corporation was primarily in a corporation that the sole asset was in real property.

Under CODE SEC 897 (C)(1) - the term United Staes real property interest means an interest in real property located in the US and under (code s897 (2) (A) the fair market value of the US real property interest equals or exceeds 50 percent of the the fair market value of its US. Based on the definitions provided by the code, Gaspar's investment in USCo is in line.

Based on the facts, there sole asset of USCo was in real property and the values of the assets exceeded the 50 percent of the fair market value.

The gain generated by the disposal will be subject to subject to US federal tax.

Sale proceeds \$3,000,000
Less: Basis \$ 900,000
Net gain before \$2,100,000
Loan repaid \$2,000,000
Net gain \$ 100,000

Basis will be (initial investment \$400,000 plus cash contribution \$500,000 = \$900,000
This gain will be taxable at the withholding tax rate of 30%.

Although there is a treaty agreement in place with Gaspar's country, the withholding will not be reduced.

Question 7

Advise on the US tax consequences of the transactions fr by Mr and Mrs Costa and their three children with regards to the foreign trust.

The trust established in Cayman Islands is a foreign trust and as such will only be taxable under Subchapter J (Code s 679 (a) - which covers the foreign trusts with one or more US beneficiaries.

Based on the facts given Mr and Mrs Costa are residents of Brazil and not the United States (US) and as in this reign will not be taxable on their foreign earned income.

The facts given state that the source of the income received during 2015 were not US sourced income and as such there will be no US tax liability arising.

Two of the children who are the main beneficiaries are also not non-resident aliens, therefore any distributions received by them will also not be taxable in the US.

The third child who attended college and medical school and now practising medicine in Texas will be deemed to be US citizen and as such will be taxable on their worldwide income.

Given that the third child will be in receipt of a third of the interest income of \$1million and dividend income \$500,000. These income will be taxable in the US and the child must include these items of income in their federal tax return for the year 2015.