THE ADVANCED DIPLOMA IN INTERNATIONAL TAXATION

June 2015

PAPER 2.10 – UNITED STATES OPTION

ADVANCED INTERNATIONAL TAXATION (JURISDICTION)

Suggested solutions

Question 1

BET Parent is a Hungarian corporation that has a Croatian manufacturing subsidiary and various African sales subsidiaries. In January 2014, it purchased all of the ownership interests in Delaware LLC to expand its operations into the United States, Canada and Mexico.

We are not told that Delaware LLC has ever elected to be treated as a corporation, so we must assume that Delaware LLC will be treated as a transparent entity under the US check-the-box rules unless and until it elects to be treated as a corporation. Accordingly, for purposes of this answer, Delaware LLC is treated as an unincorporated US branch of BET Parent.

By contrast, Croatian Sub and all of the African Subs are corporations, but it is unclear whether they are per se corporations. There is no indication that an election was filed for any of the subsidiaries.

Part 1: US Trade or Business

It appears that, prior to 2014, neither BET Parent nor any of its subsidiaries was engaged in business in the United States.

In 2014, BET Parent, through Delaware LLC, opened an office in Rochester and hired employees to work in that office. This, quite clearly, represents the conduct of a trade or business by BET Parent in the United States.

Also in 2014, Croatian Sub began to make sales into the United States. The sales were arranged for Croatian Sub by BET Parent acting as its agent. Even though all contracts were executed in Croatia and title to the goods passed from Croatian Sub in Croatia, Croatian Sub must be treated as engaged in trade or business in the United States because it had an agent in the United States with a fixed office in the United States that was conducing regular business activities on behalf of Croatian Sub in the United States.

Part 2: US and Foreign Source Income

Sales Income

Both BET Parent and Croatian Sub are engaged in the sale of goods into the United States, Canada and Mexico. BET Parent purchases goods from Croatian Sub (and unrelated manufacturers) and resells them to unrelated customers. Croatian Sub manufactures the goods itself and sells to unrelated customers (and Delaware LLC).

Croatian Sub: Manufactured and Sold Goods

For the products manufactured and sold by Croatian Sub, the income must be apportioned between sales activities and production activities. Since we are given no information about an independent factory price, we must use the 50-50 method: 50% of the income is attributable to production and 50% to sales.

The production (manufacturing) portion is sourced based on the location of the production assets. Here, we are given to believe that production takes place entirely in Croatia. Thus, 50% of all Croatian Sub's income from sales of manufactured products (i.e., $1,000,000 from sales to US customers, $800,000 from sales to Canadian and Mexican customers) is foreign source.

In sourcing the sales portion, the first issue is whether the sales are attributable to a US office or fixed place of business (OFPB). In this case, it does not appear that Croatian Sub actually has its own US office. It does, however, use Delaware LLC's employees and office to sell its products. The OFPB of an agent is attributed to a foreign principal only if the agent is dependent and either (1) has and regularly exercises the authority to conclude contracts on behalf of the principal; or (2) has a stock of merchandise from which it regularly fills orders on the principal's behalf (Reg. 1.864-7(d)). Here, Delaware LLC might be considered a dependent agent of Croatian Sub based on the fact that it is wholly owned and controlled by, and acts on behalf of, a common parent, namely, BET Parent, but the facts clearly indicate that Delaware LLC sells products in the United States that are not manufactured by Croatian Sub. Moreover, we are expressly told that the Delaware LLC employees in the US arrange sales contracts for Croatian Sub but do not have the authority to "conclude" sales contracts. Finally, the facts state that Croatian Sub transfers title to all goods bound for the United States at the port of departure in Croatia and thus has no ownership interest in any goods once they reach the United States. Under these circumstances, Croatian Sub has a strong – and probably winning -- argument that it does not have a US OFPB and that none of its sales income can be attributed to a US OFPB.

Accordingly the sales proceeds from sales to US, Canadian and Mexican customers and Delaware LLC attributable to sales activities (i.e., 50%, or $1,800,000), are foreign source.

Delaware LLC: Purchased and Resold Goods

For the goods purchased by Delaware LLC from Croatian Sub (and others) and resold in the United States, Canada and Mexico, the entire amount of income from sales is attributable to the office of Delaware LLC in the United States and the foreign disposition exception probably does not apply. Therefore all of this income ($1,400,000) is US source.

Interest Income

Besides income from sale of inventory, the other income involved here is the interest income received by BET Parent from the Bank. This is clearly US source because the Bank is a US domestic commercial bank.

Dividend income

We are told that Delaware LLC distributed profits to BET Parent in the amount of $1,200,000. These profits represent a US source "dividend equivalent amount" taxable under the US branch profits tax regime.

Part 3: Taxable Income of Croatian Sub

Croatian Sub is engaged in business in the United States but it has no US source business income and no US source FDAP income. Accordingly, Croatian Sub has no gross income subject to US tax.

The result is the same under the US - Croatia Income Tax Treaty, assuming it is the same as the US Model Treaty.

Part 4: Taxable Income of BET Parent

BET Parent is engaged in business in the United States through Delaware LLC. Accordingly, under the residual force of attraction rule, all of its US source sales income ($1,400,000) is effectively connected with its US business and is subject to US tax at the rate of 35%. The US Model Treaty does not change this result because BET Parent is engaged in business in the United States on its own behalf and not through an agent.

BET Parent has $50,000 of US interest income from the investment of its working capital in the Bank. While interest income is typically FDAP income subject to 30% withholding tax, it may be taxed on a net basis as part of the business income of a foreign taxpayer if it is effectively connected with the conduct of a business in the United States. Under the asset use test, income from the investment of a taxpayer's US working capital in a US bank account is going to be treated as effectively connected with the US business and therefore included in the US business income taxed on a net basis at 35%.

BET Parent receives $1,200,000 of distributed profits from Delaware LLC. This amount is taxable under the branch profits tax regime, which is essentially a tax on remitted profits. A statutory tax rate of 30% applies but this rate would be reduced to 5% by the US Model Treaty.

Part 5: Interest Deduction

BET Parent must compute its US interest deduction under Treasury Regulations section 1.882-5. This requires a three step computation.

First: Determine the taxpayer's "US-Connected Assets" – that is, the total value of assets that produce or could produce ECI. Here, that number is $3,450,000 (the assets of Delaware LLC).

Second: Determine the taxpayer's US-connected or "allowable" liabilities by multiplying its US-Connected Assets by its worldwide liability-to-asset ratio. Here, the liability to asset ratio is 2.44% ($0.45 million / $18.45 million) and the "allowable" liabilities are therefore $84,180.

Third: Compare "allowable" liabilities ($84,180) to the liabilities actually shown on the US books ($450,000).

In this case, the actual US booked liabilities exceed the "allowable" liabilities and BET Parent is required to scale back its actual US booked interest by the ratio of "allowable" liabilities to booked liabilities (84,180/450,000). Its interest deduction is therefore $11,972.

Part 6: Income of Executive

Executive moves to the United States in January 2014 and presumably becomes a US tax resident in short order – either because he becomes a resident alien under the immigration laws (he obtains a 'Green Card') or because he meets the substantial presence test. Assuming he becomes a tax resident in 2014, all of his worldwide income from the day of his first arrival in the United States will be subject to US tax.

The US Model Treaty will change this result only if Executive can establish that, by virtue of the fact that he still owns a house in Hungary and his family continues to reside there, he continues to be a Hungarian tax resident and, under the Treaty tie-breaker rules, has a closer connection to Hungary. If he succeeds in so relying on the Treaty, he will be taxable in the United States only on his income earned in the United States.

Part 7: Taxation of Delaware LLC as US Corporation

If BET Parent had filed an election to treat Delaware LLC as a corporation, BET Parent would not have been engaged in business in the United States and would not have been taxable in the United States. Delaware LLC, however, would have become a separate US taxpayer subject to US income tax on a net basis on its worldwide income. Since all of the income of Delaware LLC was in any event subject to tax by the United States, the practical effect of treating Delaware LLC as a corporation would not have been great.

However, there would have been a significant difference in the treatment of payments from Delaware LLC to BET Parent. As a US corporation, Delaware LLC would have been required to withhold and pay a 30% tax on every dividend paid to BET Parent (under the FDAP regime). As a US branch of BET Parent, by contrast, Delaware LLC would have been subject to the Branch Profits Tax. The Branch Profits Tax mimics but does not exactly reproduce the application of the 30% withholding tax to intercorporate dividends.

The US Model Treaty, if applicable, would reduce the applicable withholding tax rates but would not otherwise change these results.

Part 8: IRS Challenge

The facts state that Croatian Sub sells goods to BET Parent for cost plus a 9% markup. This does not comply with the US transfer pricing regulations and can be expected to generate a challenge by the IRS if it results in shifting income from the United States to Croatia.

The facts do not indicate that the Croatian Sub pays any commission or fee to BET Parent for its activities in the US in arranging direct sales to customers. This also clearly does not comply with the US transfer pricing regulations and can be expected to generate a challenge by the IRS

Question 2

Wine is a US domestic corporation that has a domestic subsidiary conducting business in the United States and several foreign subsidiaries conducting business abroad during the year 2014.

Part 1: Operations of USCo

USCo is a US domestic corporation and is accordingly subject to Federal income tax at statutory rates (deemed to be 35%) on all of its income, whether US source or foreign source. There is no distinction to be made between income from sales to US customers and income from sales to foreign customers. USCo's aggregate sales income is $12 million.

In addition to its income from sales, USCo earns royalty income in the amounts of $120,000 (due from AustriaCo) and $20,000 (due from KoreaCo). As a corporation, USCo must report its income on the accrual method and, accordingly, must accrue this income in 2014 whether or not it is actually paid in 2014.

USCo's overall net income is thus $12.14 million and the Federal income tax due on that income is assumed to be $12.14 million times 35%, or $4.249 million. However, assuming that its foreign income taxes are "income taxes in the US sense" and that they were levied on income that the United States considers foreign source income, USCo is entitled to a direct foreign tax credit of $800,000, leaving net Federal income tax of $3.449 million.

It appears that the $800,000 of foreign taxes includes only foreign taxes on operating income. USCo would also be entitled to a direct foreign tax credit for withholding taxes on its foreign- source royalty income. However, assuming that USCo has claimed benefits under the Tax Treaties with Austria and Korea, which are assumed to be identical to the US Model Treaty, royalties are exempt from withholding tax.

As a US domestic corporation, USCo is required to file a return and pay its tax on a standalone basis. However, it is likely that USCo has elected to file consolidated returns with its parent, Wine. In this case, the income and credits of USCo will appear on the consolidated Federal income tax return of the Wine group.

Part 2: Operations of AustriaCo, KoreaCo and LuxLLC

AustriaCo.

AustriaCo is a foreign corporation and, as a general rule, the income of a foreign corporation is not taxable in the United States.

Wine owns all of the stock of AustriaCo and AustriaCo is therefore a Controlled Foreign Corporation (CFC) under Subpart F. However, AustriaCo's operating income consists entirely of income from the sale of property manufactured by AustriaCo in Austria, its home country. This is not Subpart F income even to the extent that it arises from sales to affiliated purchasers such as LuxLLC. Moreover, sales to LuxLLC are made at fair wholesale value so that there should not be any transfer pricing issues under Code section 482.

The income of a foreign corporation can also be taxable in the United States under the Personal Foreign Investment Corporation (PFIC) rules, but there is no indication that AustriaCo has passive income or passive investments that could make it a PFIC.

Accordingly, none of AustriaCo's Austrian operating income is taxable to Wine in the United States in 2014.

KoreaCo.

KoreaCo is also a foreign corporation and, as a general rule, its income should not be taxable in the United States.

Wine owns only 10% of the stock of KoreaCo, so KoreaCo is not a Controlled Foreign Corporation and its income cannot be taxed to Wine in the United States under Subpart F.

There is no indication that KoreaCo has passive income or passive investments that could make it a PFIC.

Accordingly, none of KoreaCo's income is taxable in the United States in 2014.

LuxLLC

LuxLLC is treated as a branch of AustriaCo in Luxembourg for Federal income tax purposes. Moreover, since LuxLLC is engaged in purchasing property manufactured in Austria from an affiliate in Austria (AustriaCo) and reselling it for use outside of either Luxembourg or Austria, and since the tax rate levied on the income in Luxembourg is substantially lower than the tax rate imposed by Austria, the income of LuxLLC is Subpart F income of AustriaCo for Federal income tax purposes.

Therefore, the amount of LuxLLC's net after-tax operating income ($1,900,000) is treated as a deemed dividend to Wine taxable in the United States in 2014.

<u>Part 3: Distributions by AustriaCo to Wine</u>

AustriaCo distributed $500,000 to Wine in 2014 as a dividend and was deemed to distribute an additional $1,900,000 under Subpart F as a result of its LuxLLC operations.

AustriaCo also invested $100,000 in debentures of Wine on the Chicago Stock Exchange. This represents an investment of foreign earnings in US property under Subpart F and is treated as a further deemed dividend to Wine taxable in the United States in 2014.

Taking all of the above into account, AustriaCo made actual and deemed distributions to Wine in the aggregate amount of $2.5 million. Since AustriaCo had current earnings and profits in excess of that amount in 2014 ($3.2 million Austrian income + $1.9 million LuxLLC branch income), the entire amount of this distribution is a "dividend" taxable to Wine as ordinary income. There is no dividends received deduction allowed in respect of dividends from a foreign corporation.

Under the US Model Treaty, the Austrian withholding tax on dividends to an at least 10% shareholder is limited to 5%. Accordingly, it can be assumed that AustriaCo withheld $25,000 in taxes from the $500,000 dividend. This amount is allowed as a direct foreign tax credit against the US tax levied on this foreign-source dividend income. There are presumably no Austrian or Luxembourg withholding taxes levied on the deemed distributions.

As a 100% shareholder, Wine is also entitled to an indirect foreign tax credit for its share of the income taxes attributable to the dividends and deemed dividends it received. The cash dividend of $500,000 and the deemed dividends of $2 million represent 49% of AustriaCo's earnings and profits ($2.5 million divided by $5.1 million), so 49% of AustriaCo's Austrian and Luxembourg income taxes are allocated to the dividends and deemed dividends paid to Wine. Wine may therefore "gross up" its dividends by the amount of 49% times $900,000, or $441,000, and take an indirect foreign tax credit in the same amount.

Part 4: Distributions by KoreaCo to Wine

KoreaCo distributed $30,000 (10% times $300,000) to Wine in 2014. Since KoreaCo had current earnings and profits of only $240,000 in 2014 and no accumulated earnings and profits at the beginning of the year, only $24,000 (10% times $240,000) of the distribution to Wine is a “dividend” taxable to Wine as ordinary income. The balance of the distribution is treated as a return of capital and reduces Wine’s basis in its KoreaCo stock. If and to the extent that the non-dividend distribution exceeds Wine’s basis in its KoreaCo stock, it is treated as gain from the sale of the stock which is long-term capital gain because Wine has held the KoreaCo stock for more than 1 year.

Under the US Model Treaty, the Korean withholding tax on dividends to a 10% shareholder is limited to 5%. Accordingly, it can be assumed that KoreaCo withheld $1,500 in taxes from the dividend ($30,000 times 5%). This amount is allowed as a direct foreign tax credit against the US tax levied on this foreign-source dividend income.

As a 10% shareholder, Wine is also entitled to gross up its dividend income by its share of KoreaCo’s foreign income taxes ($16,000) and then take an indirect foreign tax credit in that amount against its US tax in respect of the dividends from KoreaCo.

Question 3

Part 1: Earnings and Profits as of 31 December 2014

Leopard:	A	Current Income	20,000,000.00	
100% controlled	B	(Current Taxes)	(5,000,000.00)	
	C = A + B	Current E&P	15,000,000.00	
	D	Accumulated E&P	-	
	E = C + D	Total E&P	15,000,000.00	Distribution as % of Total E&P:
	F	Distributions	(10,000,000.00)	66.67%
	G = E + F	E&P at 31/12/2014	5,000,000.00	
Jaguar:	A	Current Income	16,000,000.00	
70% controlled	B	(Current Taxes)	(4,000,000.00)	
	C = A + B	Current E&P	12,000,000.00	
	D	Accumulated E&P	-	
	E = C + D	Total E&P	12,000,000.00	Distribution as % of Total E&P:
	F	Distributions	(12,000,000.00)	100.00%
	G = E + F	E&P at 31/12/2014	-	
Lion:	A	Current Income	18,400,000.00	Distributions = 100% Leopard + 70% Jaguar
	B	(Current Taxes)	-	
	C = A + B	Current E&P -	18,400,000.00	
	D	Accumulated E&P	6,000,000.00	Associated Income Tax paid $1,800,000.00
	E = C + D	Total E&P	24,400,000.00	Distribution as % of Total E&P:
	F	Distributions	(7,100,000.00)	29.10%
	G = E + F	E&P at 31/12/2014	17,300,000.00	

Part 2: Income of Tiger

A	Dividends from Lion	7,100,000.00
B	Subpart F Inclusions	-
C = A + B	Total	7,100,000.00

Part 3: Taxes of Tiger

A	Dividend Income	7,100,000.00
B	“Gross Up”	2,308,600.000
C = A + B	Adjusted Income	9,408,600.000

D = C x 35%	Tentative US Tax at 35%	3,293,010.000	
E	Direct Foreign Tax Credit	(355,000.00)	5% of $7,100,000
F	Indirect Foreign Tax Credits	(2,308,600.00))	
G = D + E + F	Total US Tax	629,410.00	

Part 4: Investment in Tiger Bonds

A	Dividend Income	24,400,000.00	
B	“Gross Up”	7,933,333.00	
C = A + B	Adjusted Income	32,333,333.00	
D = C x 35%	Tentative US Tax at 35%	11,316,667.00	
E	Direct Foreign Tax Credit	-	No dividend in fact
F	Indirect Foreign Tax Credits	(7,933,333.00)	
G = D + E + F	Total US Tax	3,383,334.00	

Question 4

ChileFund is a foreign corporation whose sole purpose is to invest in new ventures and stocks. All of its income will be passive income and all of its assets will be devoted to the production of passive income. As such, for US tax purposes ChileFund will be a Passive Foreign Investment Company (PFIC) subject to Code section 1291 et seq.

For 2014, Roland Rivers will be taxable in the United States on the $1,000,000 in dividends that he receives from ChileFund. These will be taxed as ordinary income and, because dividends from a PFIC are not eligible for the favorable 20% dividend tax rate, will be taxed at rates up to 40%, subject to offset for any Chilean withholding taxes.

In future years, the PFIC rules may impose special interest charges in addition to the normal US income taxes that will be due with respect to any dividends Roland receives from ChileFund. In order to avoid these interest charges, which can be substantial, Roland may elect to treat ChileFund as a Qualified Electing Fund, in which case he will be taxed on his share of its earnings each year (much as if it were a partnership), or he may elect to be taxed on a mark-to-market basis with respect to his shares of ChileFund.

Question 5

Section 897(a)(1)(A) provides that "gain ... of a non-resident individual ... from the disposition of a United States real property interest shall be taken into account in the case of a non-resident alien individual, under section 871(b)(1) as if such gain were effectively connected with US trade or business." Here, the facts state that Geraint is a citizen and resident of Wales. Based solely upon the facts given, we will assume that he is a non-resident alien. We must determine for each of the alternatives whether the shares of PE are considered a United States real property interest (USRPI).

Part 1: PE holds 45% of Sun Corp`s stock

We ignore the country of Sun Corp's incorporation when determining whether PE is a USRPI. Since PE does not hold a controlling share (50%) in Sun Corp (it holds rather 45%), the fair market value of the stock of Sun Corp will be used in the determination.

First, we determine whether Sun Corp is a US Real Property Holding Corporation (USRPHC). USRPHC is defined to include any corporation (whether domestic or foreign), the fair market value of whose US real property interests equals or exceeds 50% of the sum of the fair market value of (1) its US real property interests, (2) its interests in real property located outside the US and (3) any other of its assets that are used or held for use in a trade or business.

The facts indicate that Sun Corp holds its securities portfolio for investment, so the building is the only asset to consider. Since it is considered US real property, Sun Corp will be a USRPHC, and its stock will be considered to be a US real property interest (USRPI).

Second, because the shares of Sun Corp are considered to be a USRPI for purposes of determining whether PE is a USRPHC, we must analyse all of the assets of PE. PE is not a USRPHC because the fair market value ($700,000) of its USRPIs (the fair market value of the Sun Corp shares) does not exceed 50% ($850,000) of the sum ($1,700,000) of the fair market value of its USRPIs ($700,000) and its interests in real property located outside the United States (zero) plus its other assets used or held for use in a trade or business ($1,000,000).

Since PE is not USRPHC, its stock is not a USRPI and Geraint's gain or loss on the disposition of his PE stock will not be treated as effectively connected with a US trade or business under section 897(a).

Part 2: PE holds 65% of Sun Corp`s stock

In this case, because PE holds a controlling interest (65%) in Sun Corp, PE is treated as holding a portion of each asset held by Sun Corp.

PE's portion of the Santa Monica building is determined by multiplying the fair market value of the building ($1,000,000) by 65%, giving an apportioned value of $650,000. PE is still not a USRPHC because the fair market value ($650,000) of its USRPIs (its portion of the US real estate) does not exceed 50% ($825,000) of the sum ($1,650,000) of the fair market values of its USRPIs ($650,000) and its interests in real property located outside the United States (zero) plus its other assets used or held for use in a trade or business ($1,000,000).

Question 6

According to §957 of the Code the term “controlled foreign corporation” means any foreign corporation if more than 50% of the total combined voting power of all classes of stock entitled to vote, or the total value of the stock is owned, or is considered as owned (by applying the rules of ownership of section 958(b)), by US shareholders on any day during the taxable year of such foreign corporation.

§951 provides that a US shareholder of a controlled foreign corporation must include in its income its pro rata share of the controlled foreign corporation`s Subpart F income regardless of whether that income has been distributed to the shareholder.

US shareholder means, with respect to any foreign corporation, a US person who owns, or is considered as owning (by applying the rules of ownership of section 958(b)), 10% or more of the total combined voting power of all classes of stock entitled to vote of such foreign corporation (§951(b)).

US persons owning stock in a controlled foreign corporation but not meeting the definition of a US shareholder in §951(b) are not subject to tax under Subpart F. Therefore, 11 US individuals do not have a large enough stock interest in Sub F Inc. to meet the definition of a US shareholder. Therefore, they continue to obtain the tax benefit of deferral of US income tax on such earnings unless one of the other anti-deferral regimes applies.

Question 7

A joint venture is typically treated as a form of partnership and its appears that, for Tunisian tax purposes, this joint venture is treated as a partnership and its losses are allocated between the venturers in accordance with their joint venture agreement.

Under US income tax principles, a joint venture is treated as a partnership unless it elects to be treated as a corporation, and there is no indication that this venture made such an election.

Accordingly, the US venturer (USCo) will report its share of the partnership's net loss (50% of $10 million, or $5,000,000) on its US tax return.

Question 8

In order to determine the residency of Mr. Tomas, a non-resident alien, we look to several tests: the lawful permanent resident (or 'Green Card' test); the substantial presence test; and the residency election. As the facts do not indicate that Mr. Tomas had a green card at any point in time or made any election, we will proceed according to the substantial presence test only.

The substantial presence test states that an alien individual present in the US for at least 183 days during a taxable year is a resident for tax purposes.

Alternatively, an alien individual who is (1) present in the US for at least 31 days but less than 183 days; (2) spends substantial portions of his time in the US during the 3-year period ending with the taxable year; and (3) has a closer connection to the US than to any foreign country is considered a resident for tax purposes.

Several of these terms are defined in section 7701(b): present means physical presence at any time of the day; substantial portions of his time in the US during the 3-year period ending with the taxable year means (Days in current year) + (Days in first preceding year / 3) + (Days in second preceding year / 6) ≥ 183 days.

Under this set of facts, we do not have enough information regarding Mr. Tomas` ties to the United States or Hungary, so the closer connection prong of the substantial presence test will be assumed not to be applicable.

Part 1

In 2012, 2013, and 2014, Mr. Tomas was present for 99 days, 120 days, and 145 days, respectively. All of these are less than 183 days. As such, the first substantial presence test is not passed for any of these years.

We must look to the second test. The facts state that Mr. Tomas was not present in the United States before 2012. Thus, the following calculations represent the second test:

2012
99 days + (0 days / 3) + (0 days / 6) = 99 + 0 + 0 = 99
=> not a resident under the substantial presence test

2013
120 days + (99 days / 3) + (0 days / 6) = 120 + 33 + 0 = 153
=> not a resident under the substantial presence test

2014
145 days + (120 days / 3) + (99 days / 6) = 145 + 40 + 16.5 = 201.5 days
=> a resident in 2014 for purposes of taxation.

Part 2

In 2012, 2013, and 2014, Mr. Tomas was present for 99 days, 120 days, and 115 days, respectively. All of these are less than 183 days. As such, the first substantial presence test is not passed for any of these years.

We must look to the second test. The facts state that Mr. Tomas was not present in the United States before 2012. Thus, the following calculations represent the second test:

2012
99 days + (0 days / 3) + (0 days / 6) = 99 + 0 + 0 = 99
=> not a resident under the substantial presence test

2013
120 days + (99 days / 3) + (0 days / 6) = 120 + 33 + 0 = 153
=> not a resident under the substantial presence test

2014
115 days + (120 days / 3) + (99 days / 6) = 115 + 40 + 16.5 = 171.5 days
=> not a resident under the substantial presence test

Question 9

US citizens who renounce their citizenship and move permanently abroad will be liable to a so called “exit” tax under Code section 877A (Tax responsibilities of expatriation). Section 877A(a) states that “all property of a covered expatriate shall be treated as sold on the day before the expatriation date for its fair market value”. Any net gain on this deemed sale is recognised and taxable to the extent it exceeds an exemption amount of $600.000 (indexed for inflation).

In case Mr. Gold realises his plan, he will be liable for income tax on the aggregate amount of gain that he would recognise if he sold all of his assets for cash in a taxable sale. He may, however, be able to defer paying these income taxes to the United States until he actually sells the assets in taxable sales.

Once Mr. Gold is a non-resident alien, he will be taxable, like any non-resident alien, only on his FDAP (passive) income from US sources and on any ECI (active US business income).
Once Mr. Gold is a non-resident alien, he will not be subject to US gift and estate taxes – except if and to the extent that he makes gifts or bequests to US beneficiaries.