



Association of Asian American Bankers

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U.S. – INTERNATIONAL TAX PLANNING AN ASIAN PERSPECTIVE

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Harriet Leung – hleung@rowbotham.com
Brian Rowbotham – br@rowbotham.com

Rowbotham & Company LLP
101 Second Street, Suite 1200
San Francisco, CA 94105
(415) 433-1177

www.rowbotham.com

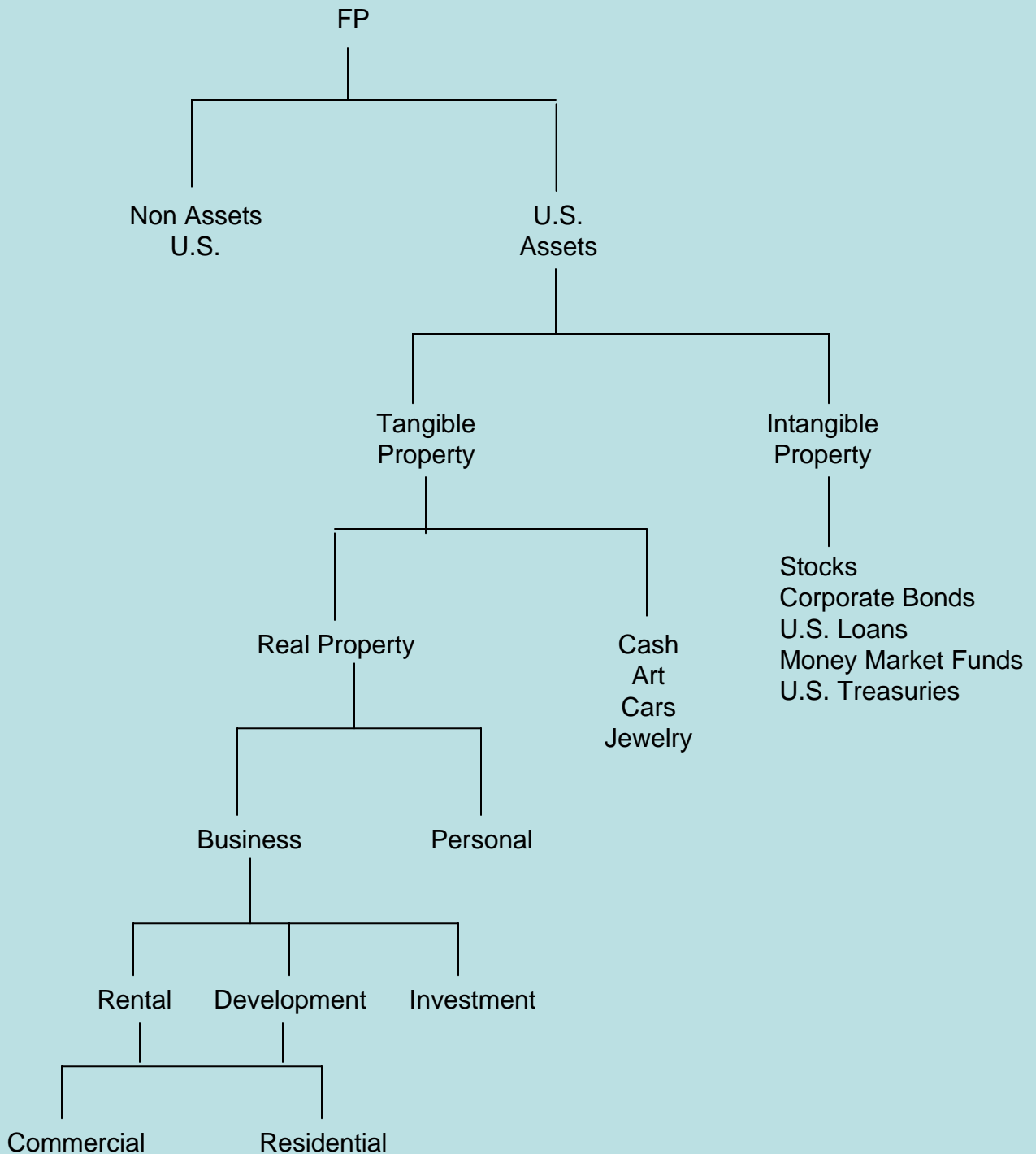


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Ownership of U.S. Assets



Income Tax Rates

<u>Individual Income Tax Rates</u>	<u>Federal</u>	<u>Average State</u>	<u>Total</u>
Ordinary Rates [single person]	35% @ \$186,825	6%	41%
Capital Gains	Maximum 15%	6%	21%

U.S. Corporations

Ordinary Rates	34%	6%	40%
Capital Gains	34%	6%	40%
Dividends Paid to FP	30% or lower treaty rate	N/A	30%

Foreign Corporations

Income Tax	34%	6%	40%
Capital Gains	34%	6%	40%
Dividends Paid to FP	N/A	N/A	N/A
Branch Profits Tax	30% or lower treaty rate	N/A	30%



Example of Individual vs. Corporate Tax Rates

Compare Sale of Investment Property

Buy Property	100
Sell Property	<u>200</u>
Gain	<u><u>100</u></u>

A) <u>Individual Tax</u>	<u>Federal</u>	<u>State</u>	<u>Total</u>
Gain of \$100	15%	6%	<u>21%</u>
 B) <u>Corporation Tax</u>			
(1) Income Tax			
Gain of \$100	34%	6%	40%
 (2) <u>Tax on Dividend Distribution</u>			
U.S. Corp. to foreign owner	30%	-0-	
(100 – 40%)	<u>x 60%</u>		
	18%		<u>18%</u>
Total Tax	(40% + 18%)	=	<u>58%</u>



Assets Subject to U.S. Gift & Estate Tax

Assets subject to tax:

Estate Tax: Property "situated in the U.S." [Section 2103]

Gift Tax: - Property "situated in the U.S." [Section 2511]

- Intangible property is excluded [Section 2501 (a) (2)]

	<u>U.S. Gift Tax</u>	<u>U.S. Estate Tax</u>
<u>Tangible</u>		
Cash	Yes	No (1)
U.S. Real Property	Yes	Yes
Art	Yes	Yes (3)
Autos	Yes	Yes
Jewelry	Yes	Yes
<u>Intangible</u>		
U.S. Money Market Fund	No	Yes
U.S. LLC	No	- - - (2)
U.S. Stocks	No	Yes
U.S. Bonds	No	Yes

(1) Special exception for cash in U.S. banks

(2) Facts and circumstances

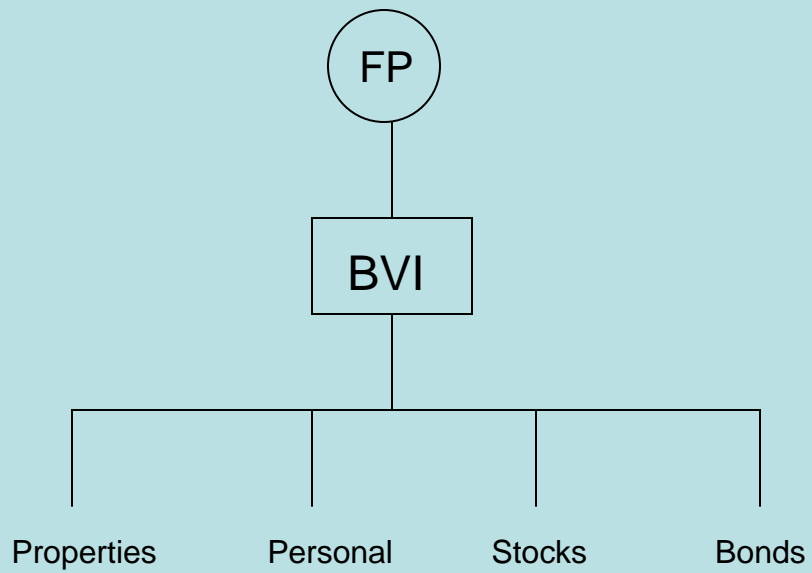
(3) Exception for art in the U.S. on display in U.S. exhibition

China

- General Rule: No gift tax
- Real Property
 - Family gifting exempt
 - 3rd party gifting has gift tax
- No Estate Tax

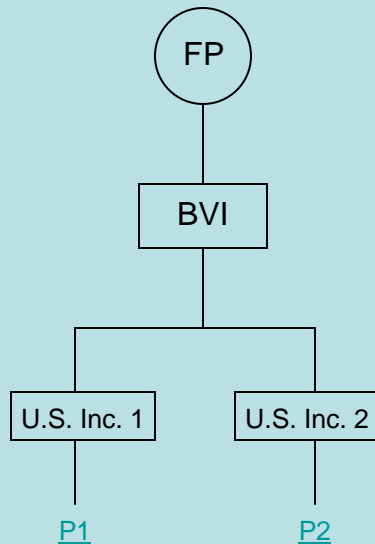


Typical “One-Stop Shop” Solution

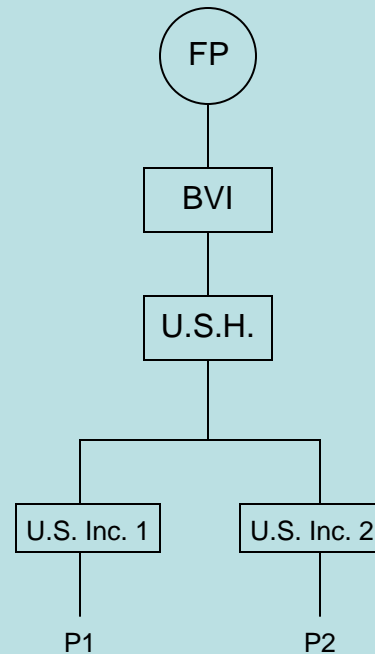


Foreign Investment in Real Property Tax Act [1980] “FIRPTA”

Alternative 1



Alternative 2

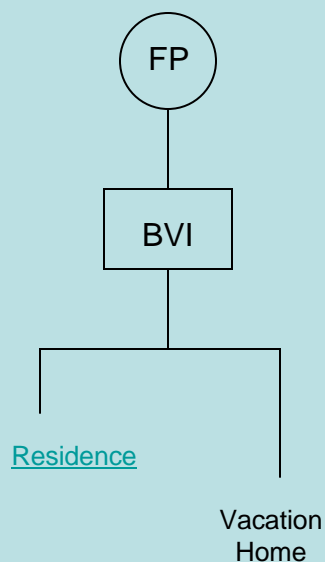


Foreign Corporation Structure

- Estate tax eliminated by foreign corporation
- Corporate tax rates on income and on gains
- Dividends paid by foreign corporation = 30% [lower treaty rate] withholding tax
- Confidentiality for ultimate foreign owner
- Sale of all U.S. property and liquidation of U.S. corporation [tax-free] avoids dividend withholding tax
 - For this reason, we usually see each U.S. property held in a separate U.S. Company [Alternative 1]
 - If U.S. holding company is used, the gains and losses are combined [Alternative 2]
 - Downside is the loss of tax-free liquidation

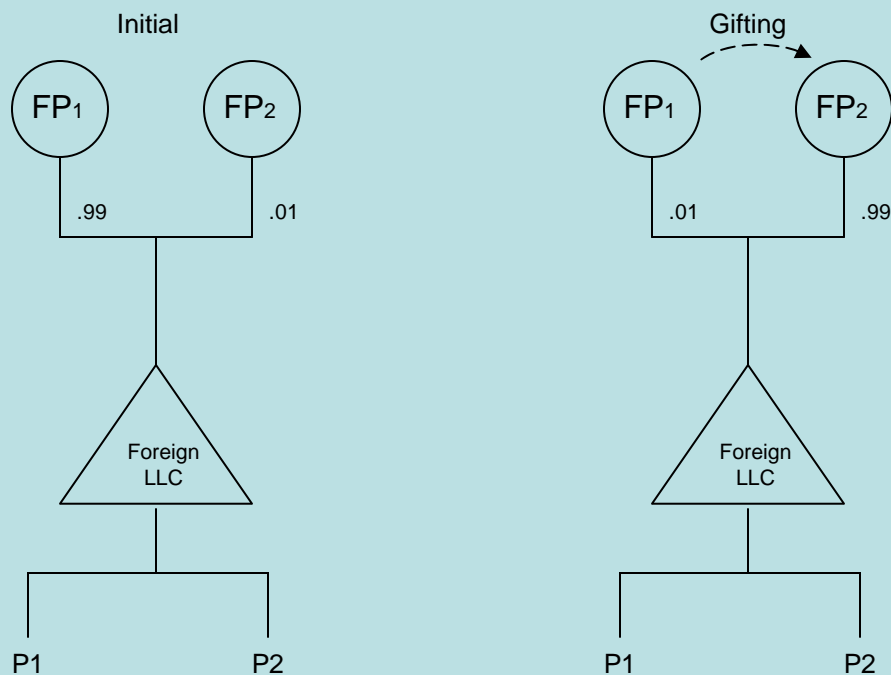


Residence Property Ownership



- Estate Tax
 - Corporate structure will generally avoid U.S. estate tax
 - Corporate sales are subject to U.S. corporate tax – 40%
- Risks
 - Section 2036 – life interest in a property included in a U.S. estate
 - Without rental activity, has FP retained property?
- Practical Answers
 - Sales by BVI companies rarely audited
 - Charge a nominal rent
 - If more than a nominal rent, then tax returns will be due or rental payments are subject to 30% flat rate of tax

Ownership Through Foreign Partnerships



Partnership Benefits compared to ownership through foreign corporation

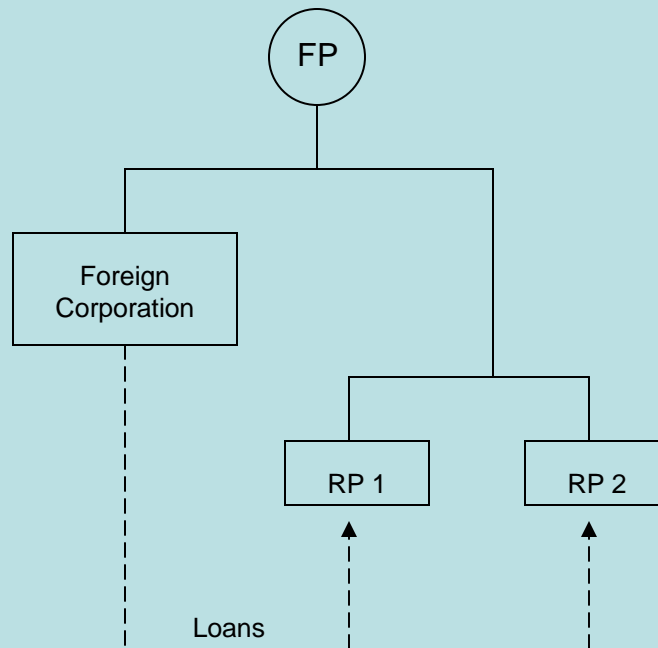
- Single Level of Income Tax
 - FP pays tax
 - FP qualifies for 15% capital gain rates
 - FP files annual returns to report U.S. income
- Partnership Interest = Intangible Property
- Partnership Interest [U.S. or foreign] is not subject to U.S. gift tax

Risk

- FP1 dies before transfer of ownership
 - Unresolved – for estate tax reporting, is each U.S. asset:
 - (a) an interest in a foreign intangible asset, or
 - (b) an interest in real property?
- Estate tax rules are unclear
- Practical approach



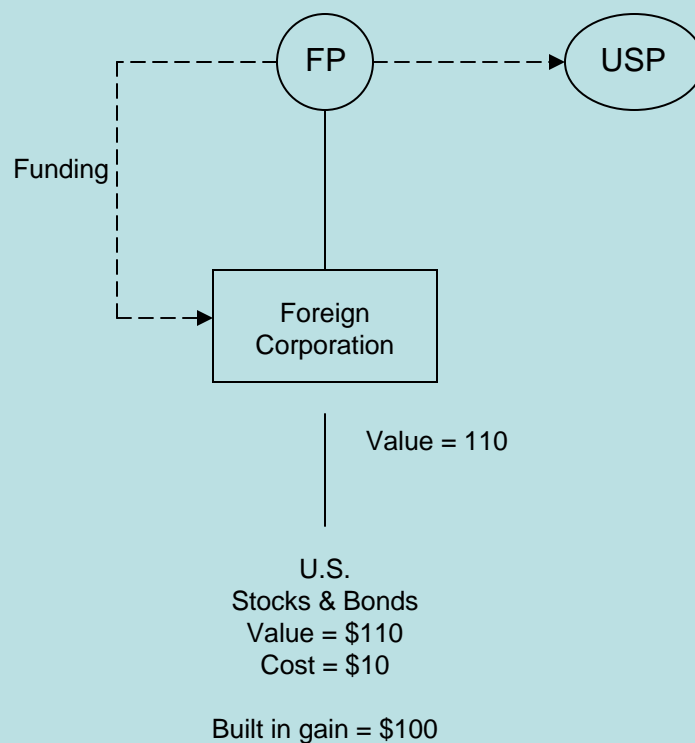
Use of Debt to Reduce U.S. Tax Exposure



- Debt will reduce the net fair market value of the U.S. property subject to estate tax
- Excessive debt to equity ratio of more than a 3:1 creates limitations:
 - Interest deductions are subject to limitations
 - Related party debt exceeding 3:1 ratio may be disallowed
 - Arms length terms and documentation required
 - interest and principal payments should be made
 - loan should be recorded as a lien against property
- Interest may be subject to a 30% [or lower treaty rate] withholding tax
- Practical limitations often limit the use of this structure



Wealth Transfers to U.S. Persons

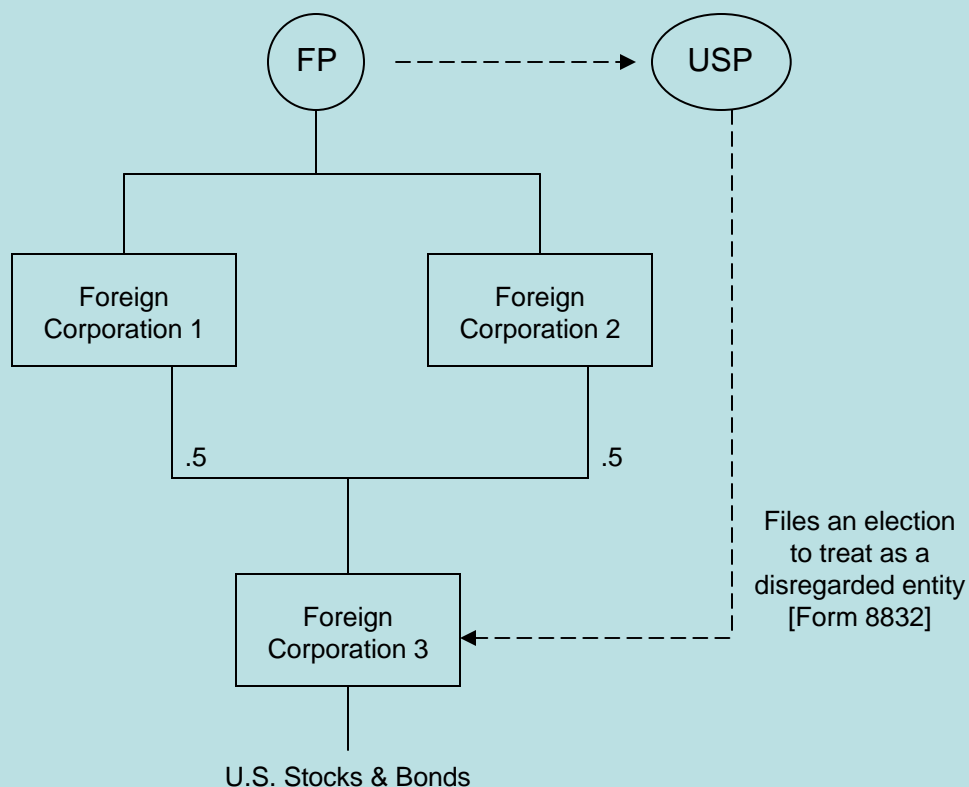


Problem with typical ownership

At date of death, USP inherits foreign corporation:

- Basis of foreign corporation steps up to \$110 [Section 1014]
- Tax basis of assets inside corporation do not step up
- Old basis carries over
- Liquidation of foreign corporation results in \$100 of dividend income to USP [Subpart F income under Section 954]
- Sale of assets by the foreign corporation results in deemed dividend of \$100 to USP [Subpart F income under Section 954]

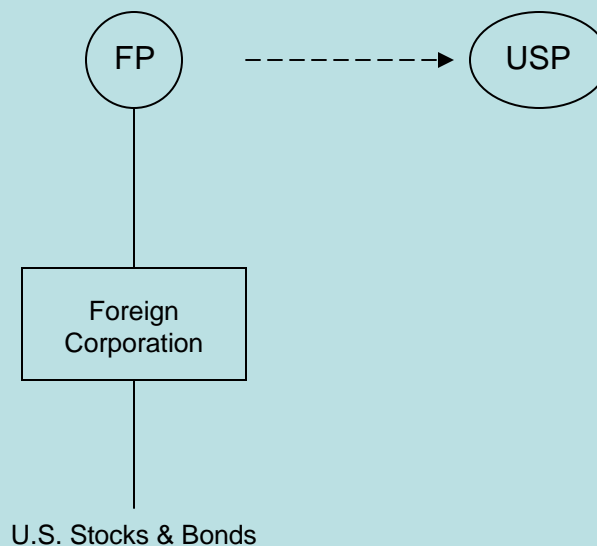
Solution # 1: Using a “Check-the-Box” Election



At date of death,

- USP inherits two foreign corporations
- The shares in Foreign Corporations (1) and (2) step up to their fair market value at date of death of FP
- USP files an election with Form 8832 to treat Foreign Corporation 3 as a disregarded entity
 - The election causes Foreign Corporation 3 to be treated as being liquidated for U.S. tax purposes only
 - The liquidation causes the assets in Foreign Corporation 3 to step up to their fair market value as long as neither (1) nor (2) owns 80% or more of (3).
 - If the election is made within 75 days of date of death, then the liquidation of (3), for U.S. tax is treated as being effective prior to death of foreign owner
- USP can now liquidate (1) and (2) and will own all the U.S. stocks & bonds at fair market value without paying any income or estate tax
- Limitation: Strategy does not work with real property.

Solution # 2: Thirty Day Liquidation



At date of death:

- USP inherits the foreign corporation with its basis stepped up to its fair market value
- Assets inside corporation will not step up
- USP now owns a “controlled foreign corporation” [Section 957]
- Sale of assets creates “Subpart F Income” = deemed divided to USP
- Exception: There is no Subpart F Income if the CFC exists for less than 30 days [Section 951]
 - Within 30 days of death, liquidate the foreign company
 - The gain from the liquidation of the CFC is no longer taxable to the USP since basis of FC stock = FMV of stock
 - Question: Can the documents and liquidation be accomplished within 30 days of the death of the foreign person?

Personal Taxation in China

Progressive rates for salaries and wages, sole proprietorship income and income from operating a business as a contractor

- 5% to 45% on salaries and wages
 - 45% on the portion exceeding RMB 100,000 monthly
- 5% to 35% on sole proprietorship income and income from operating a business as a contractor
 - 35% on the portion exceeding RMB 50,000 monthly

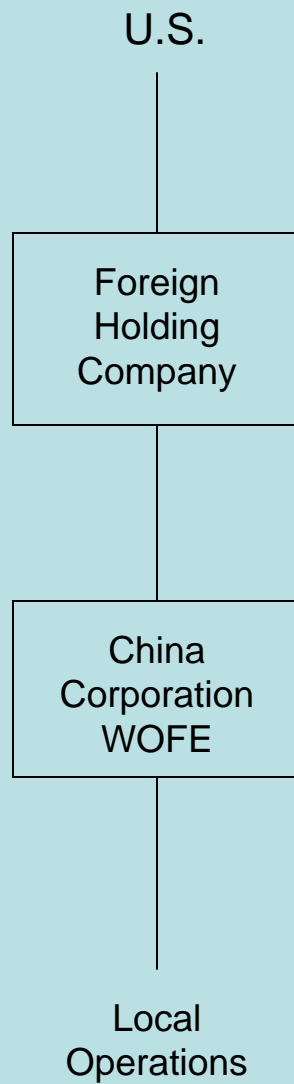
20% fixed rate for other income

Tax is typically withheld at source

No sales or local income tax

No tax deferral plans such as 401k

Investing into China





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