



TTN Conference Miami 2014

# **Not Your Father's U.S. Pre-Immigration Tax Plan**

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General Disclaimer: This discussion is not all encompassing as to the various U.S. tax issues associated with U.S. pre-immigration tax planning. The intention of this discussion is to provide a basic and general discussion as to specific case studies. You should not, and cannot, rely upon this discussion as U.S. tax advice. If there are any concerns in relation to a specific inquiry regarding a U.S. pre-immigration tax plan, please contact or engage appropriate U.S. tax counsel to advise accordingly.

# Common U.S. Pre-Immigration Planning Techniques

- Accelerate the recognition of income and gains not taxable in the U.S. (or which is subject to more favorable rates) while an NRA.
- Gifting assets to family members while an NRAD (in trust or outright) so that the value of the assets of the individual immigrating to the U.S. is at or below the inflation adjusted exemption amount for U.S. estate purposes (or the inflation adjusted portability amount in the event of spouses).
- Preparing U.S. tax based wills and trusts (including the use of a qualified domestic trust if necessary).
- Consider using irrevocable life insurance trusts.

What happens when the individual immigrating to the U.S. is not the so-called “bread winner” of the family?

We need to think outside the box and explore techniques beyond “common” planning techniques.

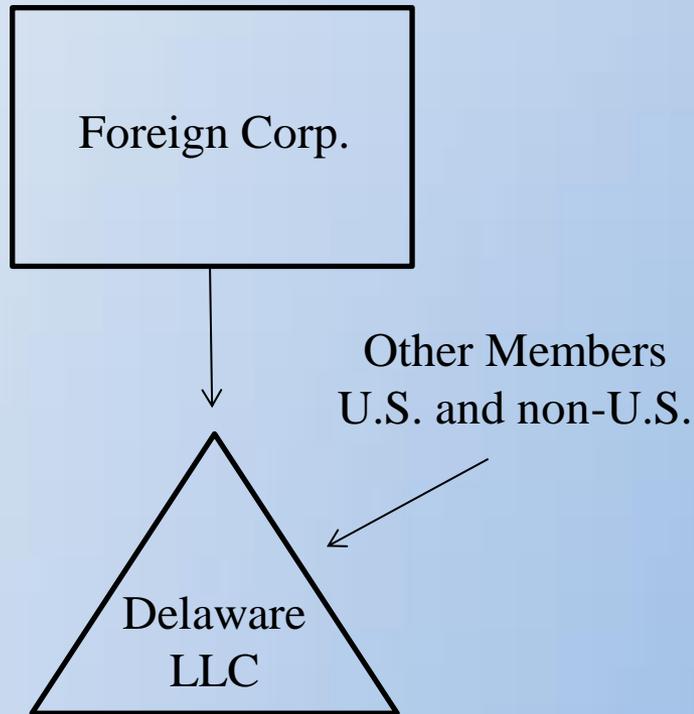
## Case Study 1:

# Use of a Trust to Purchase U.S. Business

# Case Study 1:

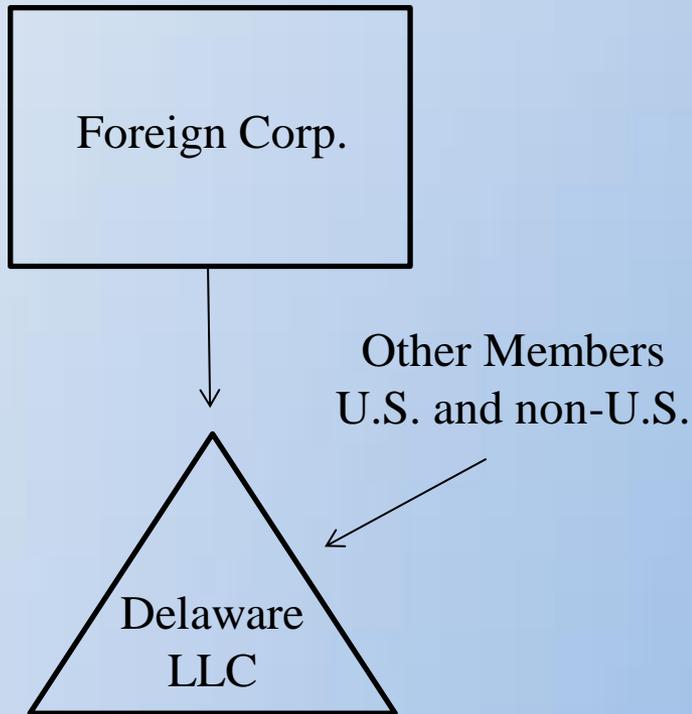
Facts presented are as follows:

- The foreign corporation is engaged in a USTB through a domestic LLC (taxed as a partnership) that has other U.S. and non-U.S. person members. The foreign corporation has a minority membership interest in the LLC.
- The foreign corporation has other non-U.S. assets and holdings and is a “per se” corporation.
- The elderly NRAD / NRA patriarch of the family owns 100% of the foreign corporation.
- The patriarch’s son is a manager and primary employee of the Delaware LLC.
- As to the foreign corporation (and other non-U.S. person members), the USTB activity generates ECI.



USTB with ECI  
(branch profits tax  
issue arising)

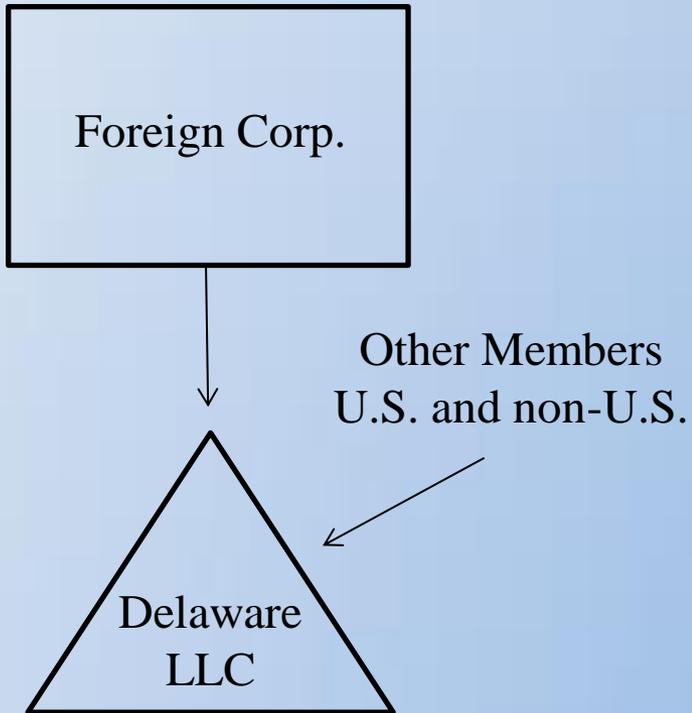
# Case Study 1:



- All equipment will be paid off at the end of the current year (Year 1).
- Projections indicate that the activities of the Delaware LLC will generate significant profits in the following year (Year 2).
- The accountants have advised that a significant branch profits tax will be triggered in Year 2 if the profit is not reinvested into the activities of the LLC prior to end of Year 2.

USTB with ECI  
(branch profits tax  
issue arising)

# Case Study 1:

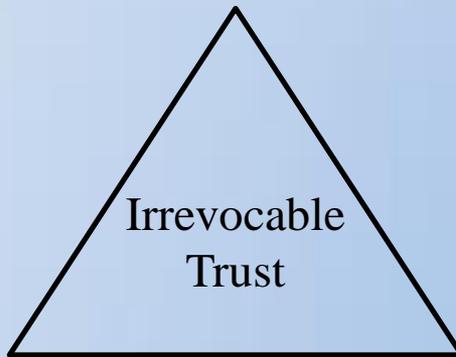


- The son has advised his father that he wants to move to the U.S. on a permanent basis in either Year 1 or Year 2.

USTB with ECI  
(branch profits tax  
issue arising)

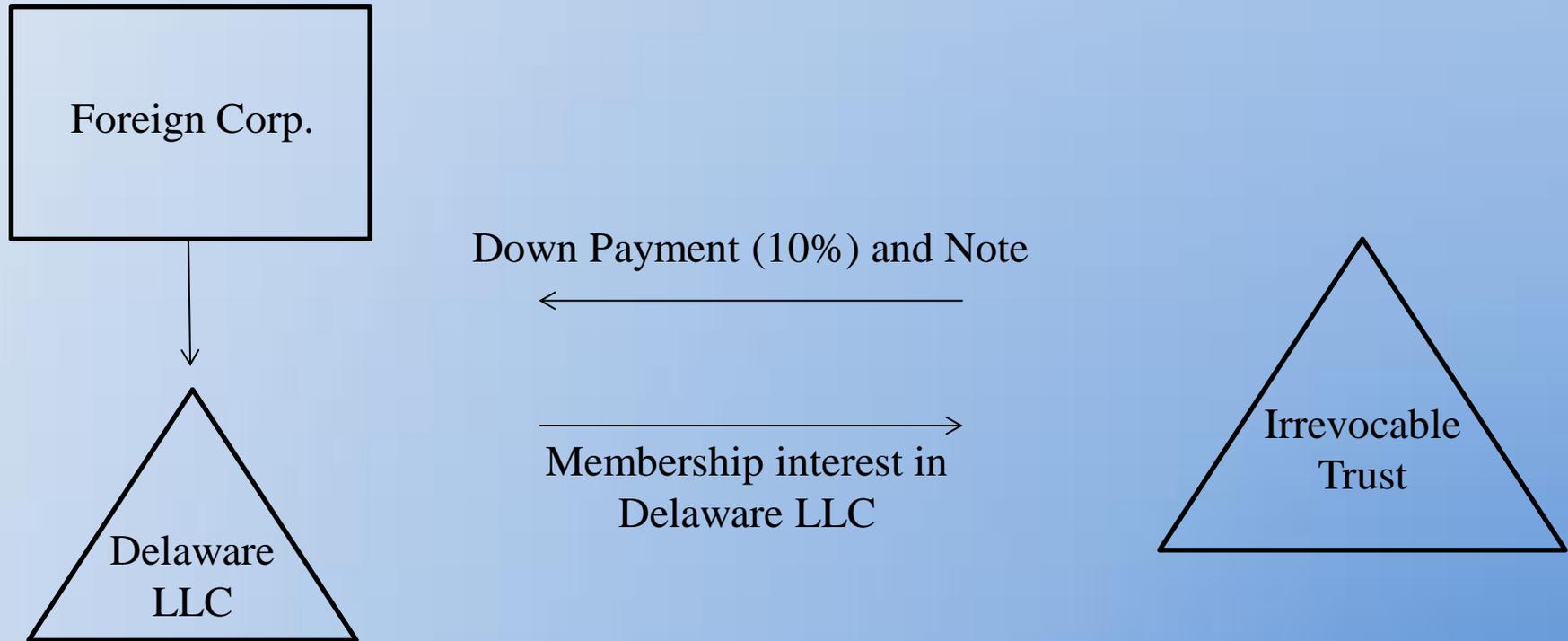
A pre-immigration planning opportunity exists, but not for the father, as the son will ultimately inherit the foreign corporation if nothing changes.

# Case Study 1:



- In Year 1, the father (as settlor) can make a cash gift (from an account outside the U.S.) to an irrevocable domestic gift trust created for the benefit of the son.
- It is advisable that the cash gift made in Year 1 be no less than 10% of the value of the foreign corporation's membership interest in the Delaware LLC (as the trust will ultimately purchase the membership interest in Year 2).
- The trust is drafted in a manner so that the assets are not subject to the U.S. estate tax upon the death of the son.
- The trust is also drafted in a manner so that the assets are protected from claims of the son's general creditors, if any.

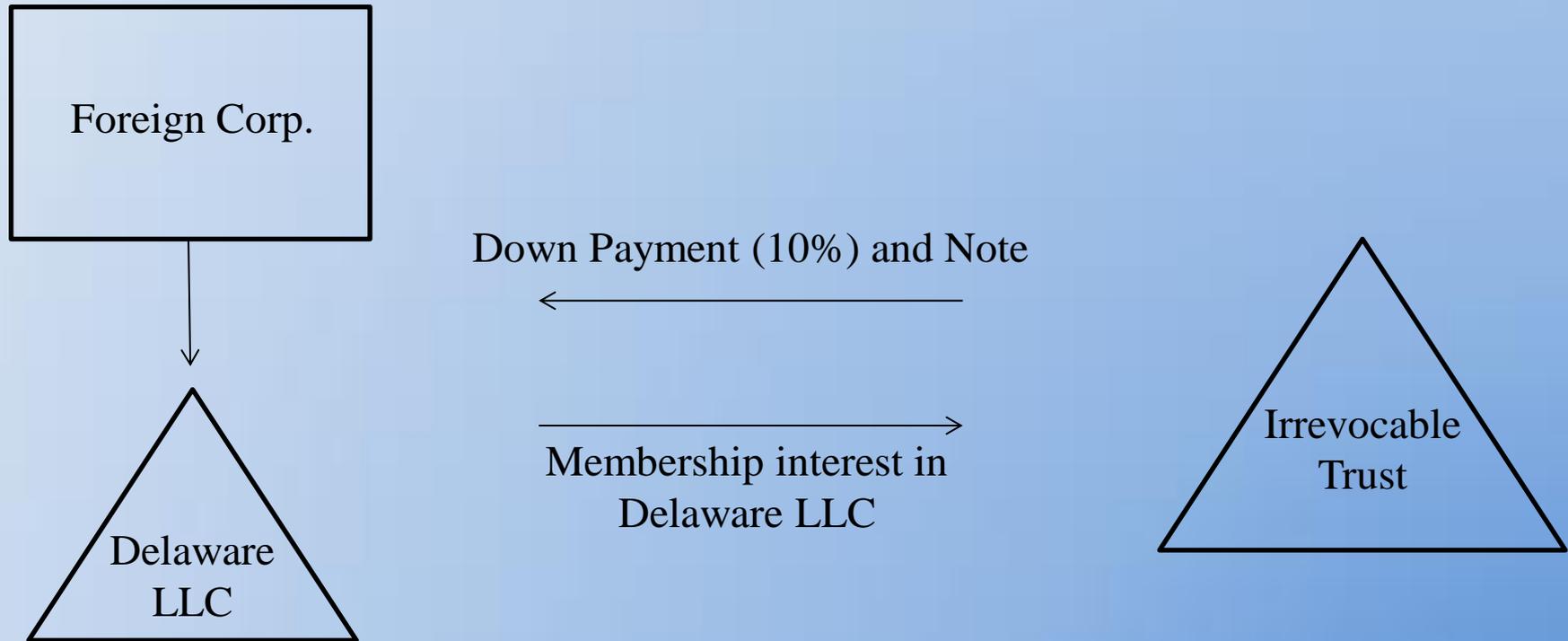
# Case Study 1:



USTB with ECI  
(branch profits tax  
issue arising in Year 2)

(This represents the Year 2 sales transaction  
after an “appropriate” amount of time has  
passed since the funding of the trust in Year 1).

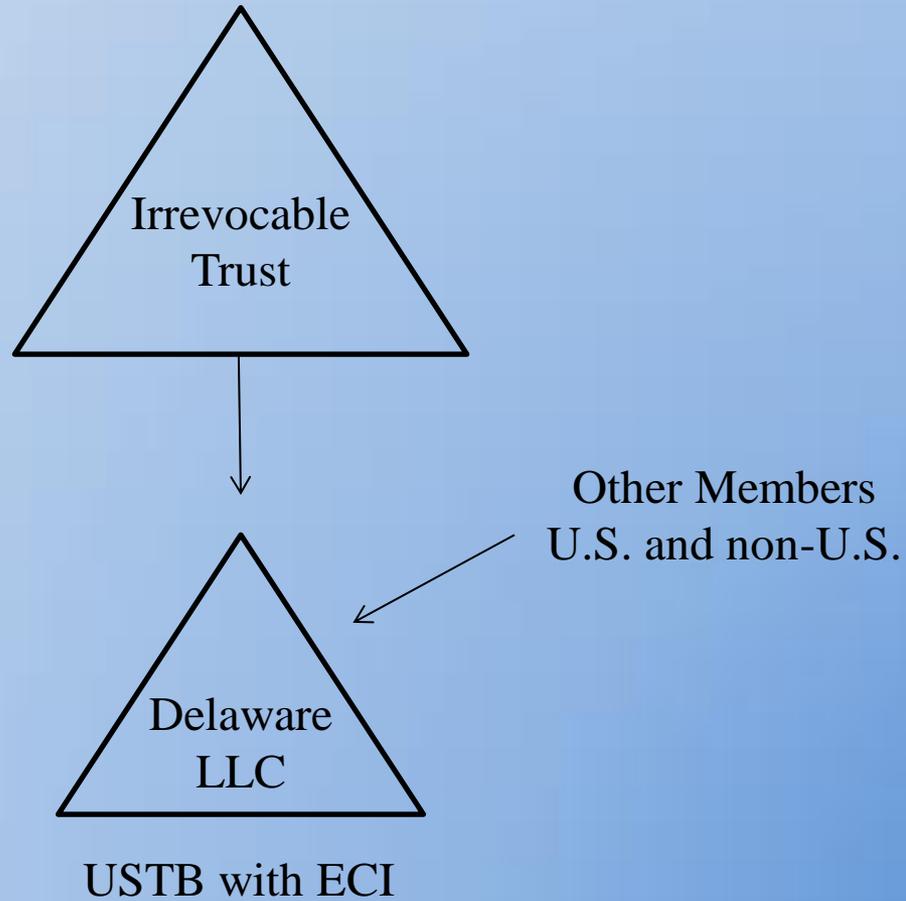
# Case Study 1:



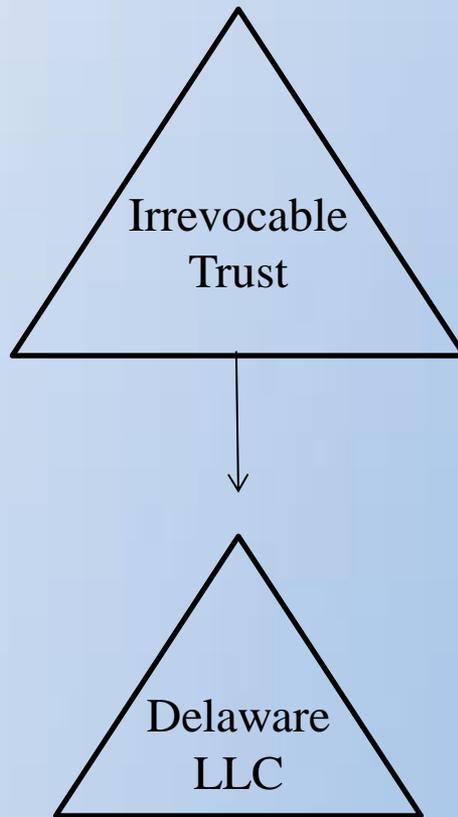
USTB with ECI  
(branch profits tax  
issue arising in Year 2)

(Consider the treatment of gain on the sale of the membership interest taking into account any applicable discounts due to fact that the membership interest being sold is a minority interest).

# Case Study 1:



# Case Study 1:



- The asset which the son manages has now been placed into an irrevocable gift trust for his benefit (beyond the reach of the U.S. estate tax and beyond the reach of general creditors).
- The son will not inherit the membership interest in the Delaware LLC via the inheritance of the “per se” foreign corporation (as such an inheritance would have adverse U.S. tax consequences when attributable to a U.S. person).
- So long as the foreign corporation satisfies the requirements of the complete termination rules, the potential branch profits tax issue in Year 2 will be avoided.
- Additional time has been bought to deal with the other non-U.S. assets and holdings of the foreign corporation so as to plan properly for the future inheritance by the son.

## Case Study 2:

Pre-immigration trust planning when one spouse moves to the United States and the facts “force” you to use an irrevocable trust....

## Case Study 2:

Facts presented are as follows:

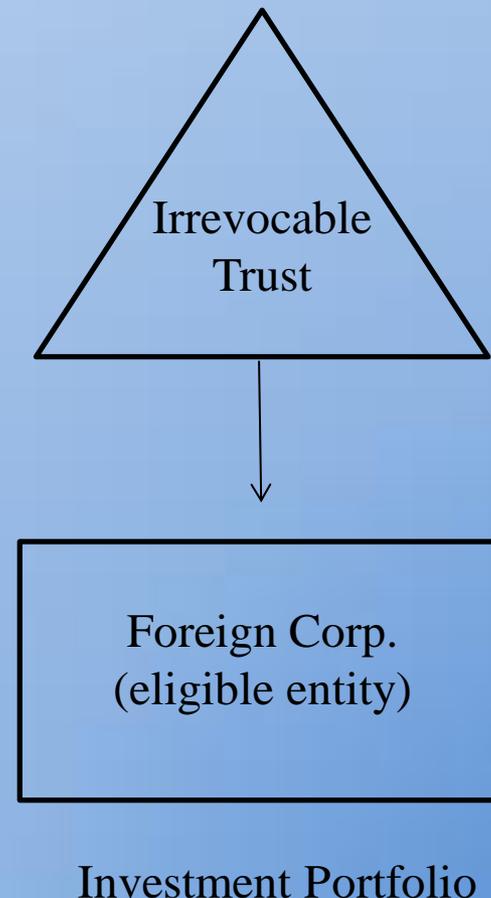
- Due to economic, educational and security concerns in the “home” jurisdiction, the wife and children must make a permanent move to the United States.
- The husband must remain in the home jurisdiction to maintain the family business and take care of his elderly father.
- The real family wealth is separate (non-community) property from the husband’s side of the family.
- Due to wife’s willingness to move to the United States and leave her husband behind, she has asked that her financial and economic stability be addressed now and in a manner that her husband cannot unwind.
- Both parties are agreeable to all matters.

A pre-immigration planning opportunity exists, but not for the father, and the family wants to minimize its U.S. tax exposure.

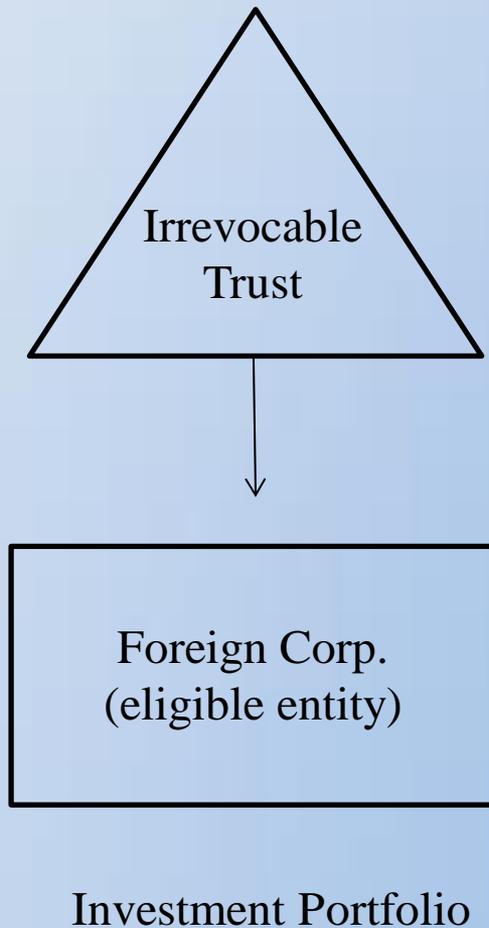
## Case Study 2:

The proposed structure...

- The NRAD / NRA husband (as settlor or grantor) funds an irrevocable gift trust with the shares of stock in a foreign corporation.
- An investment portfolio is held in the name of the foreign corporation.
- The intention is that the trust be held only for the benefit of the now U.S. person wife (and the U.S. person children), subject to the U.S. tax planning discussion that follows.

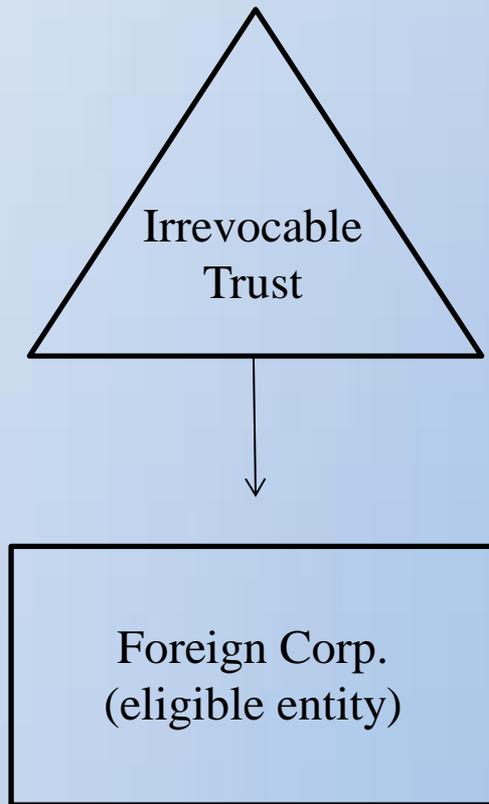


## Case Study 2:



- For U.S. income tax purposes the trust is made a grantor trust by planning for § 672(f).
- If irrevocable, grantor trust status is only achieved if distributions during the grantor's lifetime are to the grantor (husband) or the grantor's spouse (wife).
- Due to the assurances the wife wants, the wife will be the only beneficiary of the trust during the husband's lifetime. Although the wife is the only beneficiary during the husband's lifetime, this structuring will still meet the requirements of § 672(f)(2) so that the husband is treated as the owner for U.S. income tax purposes.
- If the wife passes before husband, the trust is drafted so that the assets revert outright to the husband as the wife is confident the husband will take care of their mutual children.

## Case Study 2:



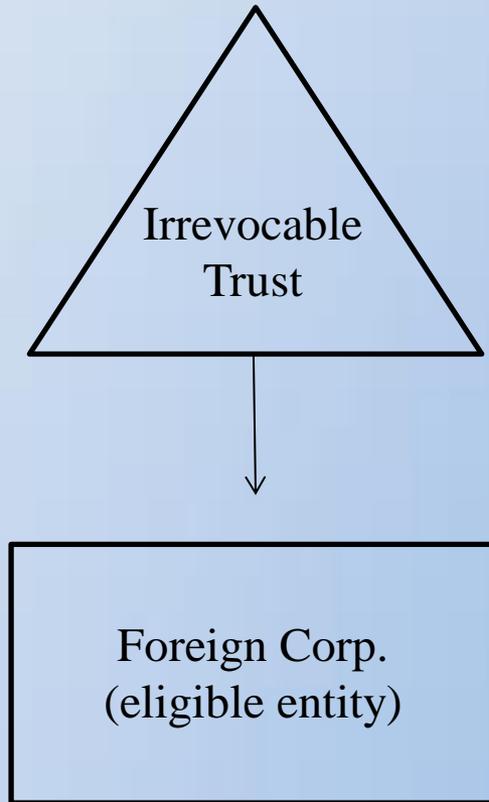
What if U.S. situs assets are part of the holdings?

Due to the reversion interest husband has in the assets of the trust, the use of the foreign corporation should help avoid U.S. estate tax issues upon his death.



Investment Portfolio

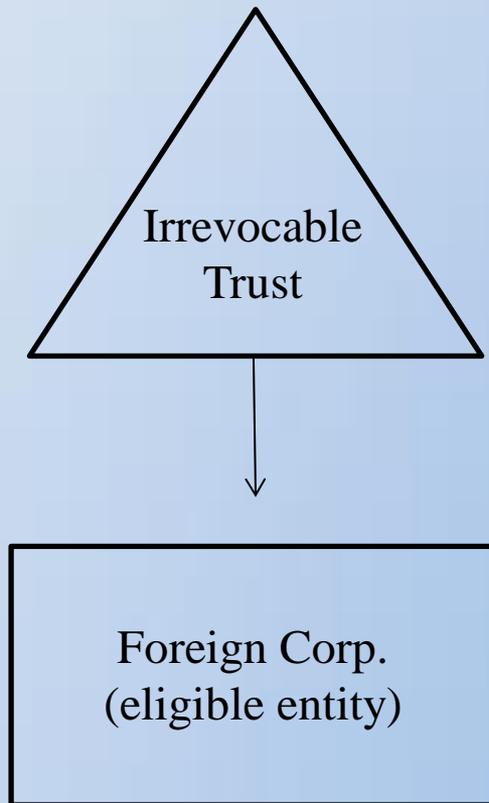
## Case Study 2:



Investment Portfolio

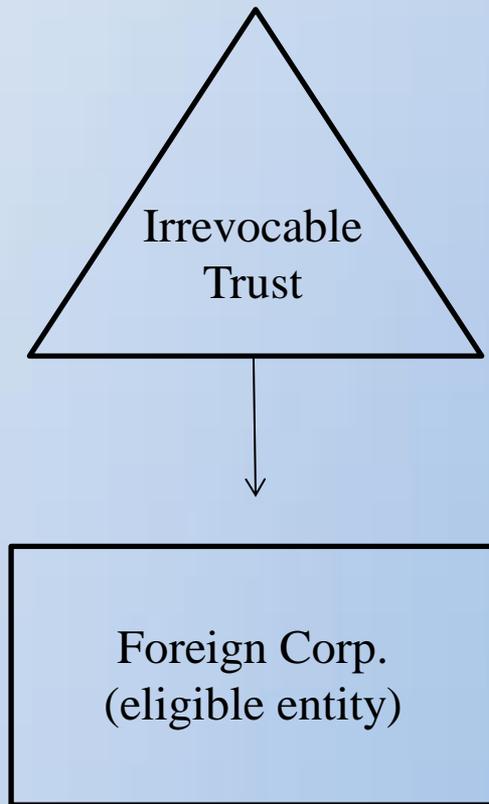
The foreign corporation will be a CFC if the trust is a “domestic trust”. Consider the disclosure of the subpart F income if a Form 5471 has to get filed. Even if the foreign corporation has CFC status (due to ownership being held directly in the name of a U.S. person, the domestic trust), and reporting is required, the trust should still remain a grantor trust as to the husband if an exception to § 672(f) is satisfied, and, thus, there should be no U.S. income tax.

## Case Study 2:



- Consider making the trust a foreign trust (by failing either the “court test” or the “control test”) so as to potentially avoid CFC status and the related Form 5471 filing. In this regard, consider the separate application of the indirect and constructive § 958 and the related Regulations to an irrevocable but grantor trust with U.S. person beneficiaries.
- If the trust is a foreign trust, consider the fact that there may be no requirement to file the Form 3520 in relation to the initial gift to the trust.

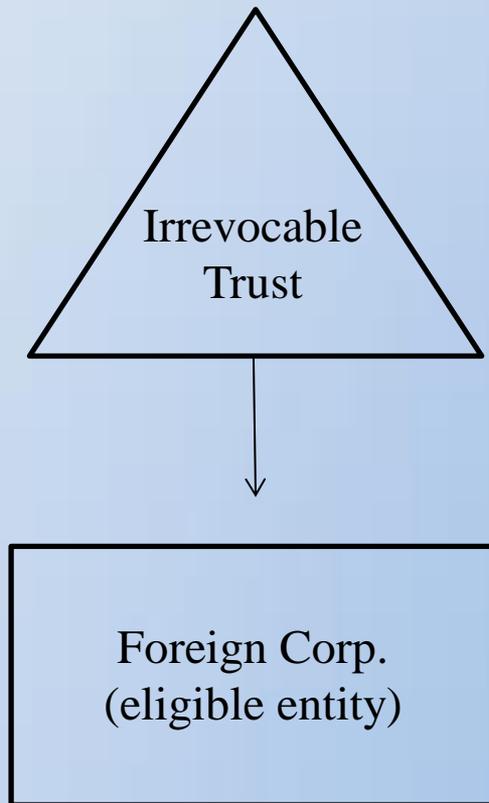
## Case Study 2:



Investment Portfolio

- In this Case Study 2, a State of Florida trust agreement is used; however, the trust is foreign for U.S. tax purposes because a non-U.S. person relative other than the husband has the power to appoint and remove the trustee (thus making the trust fail the “control test” as all substantial decisions are not in the hands of U.S. persons).
- The trust is drafted so that the control test would be satisfied on and after the death of the husband (e.g., the power to remove and appoint trustees would be drafted in a manner so that U.S. persons control all substantial decisions). In this regard, the trust becomes a domestic nongrantor trust on the death of the husband.

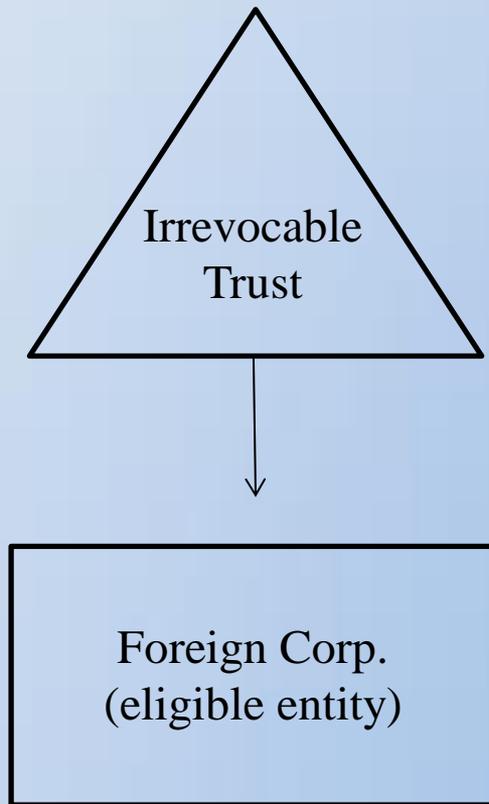
## Case Study 2:



Investment Portfolio

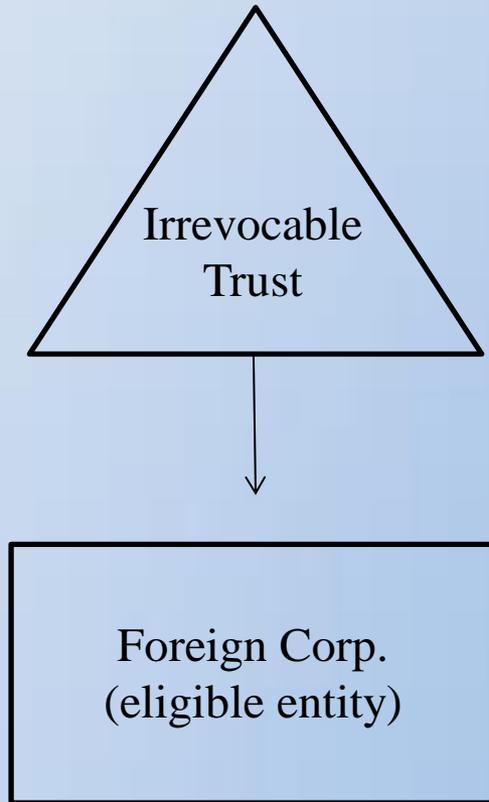
- Upon the death of the husband (the settlor), the trust will become a domestic nongrantor trust with U.S. person beneficiaries as noted before.
- Consideration should be given to causing a deemed liquidation of the foreign corporation (via the “check-the-box” election found in Reg. § 301.7701-3) by electing status as a disregarded entity. This should help avoid application of the controlled foreign corporation and passive foreign investment company anti-deferral regimes after the husband's death (when ownership will clearly be attributable to U.S. persons).

## Case Study 2:



As the husband will not have a revocation or amendment power, a basis adjustment under § 1014 will likely not be available. How can we plan as to the unrealized appreciation as to the trust's ownership interest in the foreign corporation? How can we avoid the tax on the potential gain as a result of the deemed liquidation?

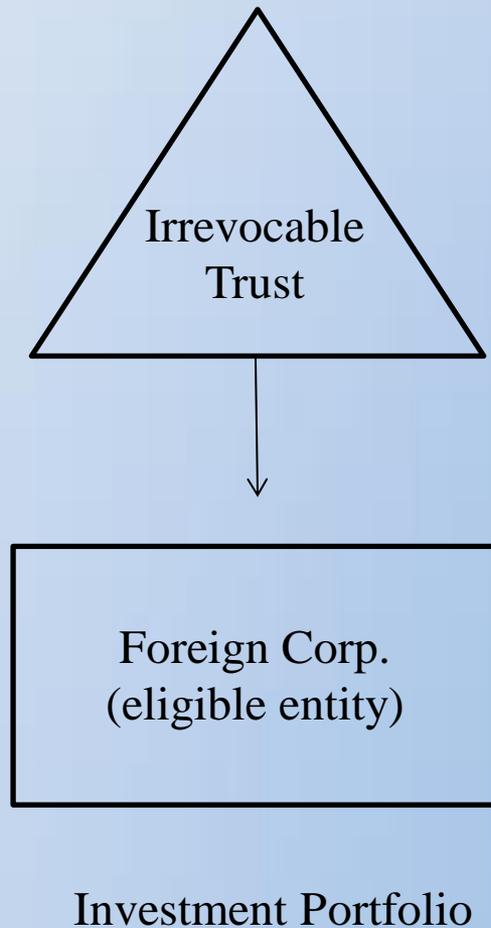
## Case Study 2:



- Consider annual “cleansing” techniques to increase the trust’s basis in the foreign corporation, or, in an effort to maintain historical cost basis, consider an annual distribution to the trust, and then to the wife, of all income and realized capital gains. Both methods would be used in an effort to mitigate the effects of the deemed liquidation.
- In the event the foreign corporation was considered a controlled foreign corporation during the husband’s lifetime (due to the application of § 958), has cleansing already occurred?

Investment Portfolio

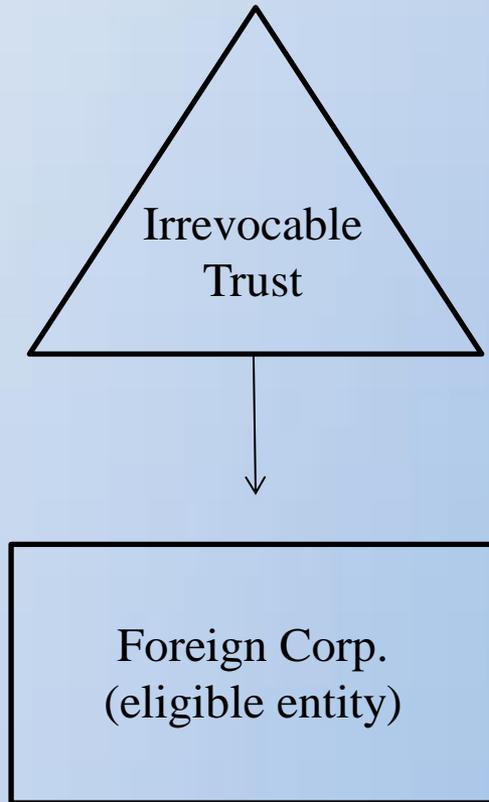
## Case Study 2:



What if husband moves to the U.S. and becomes an RAD / RA prior to his wife's passing? Additional U.S. pre-immigration planning would need to be considered for husband. The following would be issues to consider:

- Does the husband want to remain the owner for U.S. income tax purposes via the grantor trust rules?
- The foreign corporation would likely need to elect disregarded entity status and timing would need to be considered.
- The husband may want to disclaim his reversionary beneficial interest in the trust prior to becoming an RAD due to likely U.S. estate tax issues (as the foreign corporation would no longer shield from the U.S. estate tax).

## Case Study 2:



What if there is a decree of divorce or of separate maintenance? Consider the application of § 672(e) if said decree occurs prior to the formation of the trust versus after the trust structure is in place.

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