GOING WEST

Your company, or your partner's, has asked you to do a few years in the USA. Maybe you are following a personal connection, or just want to try a different experience. Before heading to the US there are a number of things you need to do to tidy up you UK situation, and many more to get yourself properly establish in the US.

LEAVING THE UK

Departure from the UK tax system is at the end of the last tax year in which you meet the criteria for tax residence. However, if you leave the UK to take up full time employment in another country you can claim a split year and exclude from your last UK tax return any income arising after the first day of work in the new country. If you don't need to file a UK tax return for that year you can us a form P85 to claim repayment of any excess tax withheld from employment in the UK.

If you have ongoing UK sourced income, such as rental property, then you should continue to file returns for that income in the normal way. There is no need to file returns for income from non-UK sources while you are non-resident.

OTHER TAX CONSIDERATIONS BEFORE LEAVING THE UK

- **Should you sell your house?** Often when moving to another country the length of time that you will be away is uncertain. One way of dealing with that uncertainty is to retain your old home and rent it out until you return. If you do this in the UK then you will retain the tax free benefit of your house as your Principle Private Residence for the first nine months after you leave. After that any gain will have to be split between your time in actual residence plus the final nine months and the period for which you were not in residence. The proportion of the gain while non-resident will be subject to capital gains tax. Since April 6, 2015 property located in the UK owned by non-residents has become subject to UK Capital Gains Tax. If you do continue to rent out your property then you will have to file a UK tax return. Under the Making Tax Digital initiative, from April 2023 landlords will have to make an online submission of rental income and expenses, and pay tax on account, at the end of each quarter.

- **Rationalizing your investments.** If you hold on to your UK investments, and then sell them generating a capital gain when you are resident in the US, then that gain will be taxed at US rates, which are usually lower than UK rates. It may make sense to realized significant gains after you leave the UK. The one exception to this is shares held in an ISA. The US does not regard these as tax exempt arrangements and will tax dividends and capital gains within an ISA. It therefore makes sense to crystallize any gains in your ISA portfolio before you leave the UK. If you expect to be in the US for a long time, it may make sense to get the investments out of the ISA wrapper before you go.

  If you have your assets in UK pooled investment funds (unit or investment trusts, ETF's, hedge funds etc.) you should consider unwinding the arrangements before becoming resident in the US. They are regarded in the USA as Passive Foreign Investment Corporations (PFIC). Income from a PFIC not only suffers a heavy penalty rate of US tax the compliance paperwork is demanding with heavy penalties for errors in reporting. Direct ownership of shares and bonds may be a more tax efficient option. When you have established residence in the US you can invest in the full range of US investment vehicles, including IRA's, without regard to the UK tax consequences. However, you do need to bear in mind that you may need to unwind some of these arrangements when you leave the US to avoid the non-reporting fund penalties on capital gains when you get back to UK residency.

- **Your pensions.** Fortunately, there is a treaty between the UK and the US that recognizes the treatment of pension funds, including 401(k) and similar funds (but not IRA's), and does not apply these tax rules to investments held within such funds.

- **Social Security.** The US and UK have a treaty (Totalisation Agreement) on Social Security. If your UK employer sends you to the US for a fixed period of less than 5 years then you stay in the UK system and the UK employer pays into UK National Insurance for you and provides the US employer with a certificate excluding you from paying US Social Security contributions. In all other cases you stop paying into UK National insurance and become liable for US Social Security contributions. If necessary, years of contributing into the US Social Security scheme can be used when determining eligibility for UK National Insurance benefits.

ONGOING UK ISSUES

If you have been in the US far longer than you originally planned and have no current plan to return you may have left some tax issues behind in the UK that need attention. For example:

- You have let out your old home or other properties
- You have pension funds that are dormant
- You have ISA's or other tax advantaged investments
- You may be in line for a significant inheritance or gift or planning to make one.

There have been significant changes in UK legislation on the taxation of property income and capital gains, and there are important changes in the reporting requirements for property income soon to be implemented.

There have also been changes to UK pension regulation, and you need to understand how the new rules interact with your US pension arrangements, and possibly take the opportunity to move pension assets outside the UK for the longer term.

Recent changes to UK law on residence and domicile have important implications for assets caught by inheritance tax.

ARRIVING IN THE USA

RESIDENT OR NONRESIDENT

Whether you will be regarded as a resident or non-resident depends upon the citizenship and visa that you hold, and the number of days that you spend in the US. There are three main categories:

- US Citizens and Green Card holders must always file a standard 1040 tax return whether they are physically resident or not.

- For all others there is "substantial presence" test, based on the number of days in the US. The test takes the number of days in the current tax year (provided it is over 31), plus one third of the days in the US in the preceding year, plus one sixth of the days in the year before that. If the total of this calculation is 183 days or higher then you are considered as resident for that year and are taxed on your worldwide income.

- Anyone else receiving income from the USA is considered a non-resident taxpayer, and is taxed on US source income only, filing a 1040NR form.

There are a few variations on this:

- If you become US resident, or if you cease to be US resident during a tax year you are classified as having Dual Status, and file both a resident and a non-resident part of your tax return.

- If you have a student (F or M) or teacher/researcher (J) visa then for the first 2 to 5 years of residence, while attending the course, are disregarded in the substantial pretense test, meaning that you are taxes as a non-resident.

- Special rules apply to diplomats and employees of international organizations and their families.

SOME CHARACTERISTICS OF THE US TAXATION SYSTEM

- The US is a multi-layered system of taxation. In addition to Federal Taxes, most States, and some Cities and Towns, levy taxes on income and estates, as well as State and Local Sales and Property taxes. Only six States (Florida, Texas, Washington BC, South Dakota, Wyoming, and Alaska) do not have some form of income tax. States base their taxable income on the Federal code, but then often add local variations to it. The total tax bill that you will face will depend on where you live, and where you work.

- The US tax year is the calendar year. For personal income tax the due date for filing and paying any tax due is April 15th of the following year. Companies and partnerships must file by March 15. It is possible to get an extension to file until October 15, and people residing outside the US on December 31 have an automatic extension until June15. However, these extensions only give extra time to file. You need to pay your best estimate of taxes due before April 15 to avoid late payment penalties. State and City income taxes are paid to the same timetable.

- There is a withholding system for employment income, but it is very crude in its application. It usually results in an over withholding so tax has to be claimed back through the tax return. However, if you have multiple jobs, or you change jobs during the year, it can also result in too little being withheld, and a balancing payment is required with the tax return. For non-employment income such as business trading income, dividends, interest, and rental income, there is an Estimated Payments system, with (approximately) quarterly payments on account. It is up to the taxpayer to decide how much is due at the end of each quarter, with the balance owing or refundable being dealt with through the tax return.

- State taxes on employment and business are paid in the state in which the work is done. That means if you have a job that involves a lot of working away from home in other states then you may have to file several state returns each with the portion of your employment or business income earned in that state. The state in which you are resident also taxes you on all your income, but then gives you credit for the taxes paid to the other states in which you earned income. However, the States are not parties to the US Federal Tax Treaties, and generally do not give credit for taxes paid outside the US on income earned in other countries. In high tax locations like New York City and California, managing your state taxes is almost as important as managing your Federal taxes. For optimal tax management your location with the US is an important choice.

- In addition to income tax, if you are employed or self-employed you will also have to pay contributions to Social Security (6.2% of your income up to $128,400) and Medicare (1.45% on all your income). The employer pays the same amount to match the employee contribution. Self-employed people pay both the employee and employer portions, then called Self Employment Tax.

- The whole tax system organizes its records around Social Security numbers for individuals and Employer Identification numbers (EIN) for businesses. If you didn't apply for one with your Visa or Green Card application, one of your first ports of call on arrival in the US should be to the local Social Security Office to apply for one. Not only tax records, but almost all official services, banking, and healthcare work on the assumption that you have one, although they can't insist on it.

IF THIS LOOKS LIKE YOU CONTACT US FOR A CONFIDENTIAL REVIEW OF YOUR SITUATION, AND TO DEVELOP A PLAN TO MANAGE IT