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What to expect in 2013

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As 2012 draws to a close, advisers to international families know that the US tax laws will change and the implementation of expanded reporting obligations will continue. President Obama and Congress are discussing further tax law changes. In this uncertain environment, advisers do their best to help families make investment and succession-planning decisions involving complex questions of law, tax and business planning and take the necessary steps for passing wealth to the next generation.

State of play

Gift, estate and generation-skipping transfer tax rates and exemptions will change

As previously reported, the current US transfer tax rates and exemptions are scheduled to expire on December 31 2012. As yet, Congress has taken no action to stop the decrease in the aggregate transfer tax exemption from $5.12 million to $1 million and the increase in the top transfer tax bracket from 35% to 55%, effective January 1 2013 (for further details please see "Changing estate and gift tax laws and international family succession planning").

Increased reporting will continue

US individuals with foreign investments who receive large gifts or bequests from foreign persons or distributions from foreign trusts will continue to have significant filing requirements in 2013. At a minimum, they will have to file the following:

- Form 3520 – Annual Return to Report Transactions with Foreign Trusts and Receipt of Certain Foreign Gifts;
- Form 8938 – Statement of Foreign Financial Assets; and
- Form TD F 90-22.1 – Report of Foreign Bank and Financial Accounts.

Further forms are required with regard to certain foreign corporations, passive foreign investment companies and foreign partnerships. Reporting obligations are not necessarily triggered solely as a result of ownership, but can be required when a US person has signature authority or serves as a director or officer (for further details please see "IRS releases new form to report specified foreign financial assets").

Foreign Account Tax Compliance Act reporting start dates/deadlines delayed – again

The Foreign Account Tax Compliance Act (commonly known in the United States by its acronym, FATCA) provisions of the Hiring Incentives to Restore Employment Act 2010, which added the Form 8938 reporting requirement, also require certain foreign financial institutions to report to the Internal Revenue Service (IRS) information on accounts held by US persons. A 30% withholding tax will be imposed on certain payments to:

- foreign financial institutions that do not enter into a form agreement with the IRS and are not otherwise exempt; and
- persons not providing identifying information or not waiving customer privacy laws that would prevent reporting to the IRS.

The IRS has again changed the start date for these new rules. Participating foreign financial institutions are now required to:

- implement new client account procedures and due diligence by January 1 2014 – an extension of six months from the previous start date of July 1 2013; and
- complete due diligence on pre-existing foreign financial institution client accounts by June 30 2014 – an extension of six months from January 1 2014.

In regard to withholding, the implementation of the Foreign Account Tax Compliance Act withholding on gross proceeds from the sale of property that produces US source interest or dividends has been delayed until January 1 2017. In addition, the deadline for participating foreign financial institutions reporting for periods ending in 2013 and 2014 has been delayed until March 31 2015.

IRS will also gather information on non-US individuals

In addition to requiring foreign financial institutions to identify US account holders and report information about those accounts to the IRS, in April 2012 the IRS issued final regulations requiring US financial institutions to report interest earned by non-US account holders on deposits held with that institution. From January 1 2013 any interest in excess of $10 earned by a non-resident alien on a deposit maintained with that financial institution will be reported to the IRS. The actual reporting will start in 2014 in respect of the 2013 calendar year. When issuing the final regulations, the IRS noted that gathering this information would facilitate intergovernmental cooperation on Foreign Account Tax Compliance Act implementation by better enabling the IRS, in appropriate circumstances, to reciprocate by exchanging information with foreign governments for tax administration purposes.

Proposals

Much attention has been given to the debate on income tax rates and brackets, but the Democrats and Republicans are also divided over estate and gift taxes. Most Republicans and some Democrats would like to see an extension of the existing $5.12 million transfer tax exemption and 35% top transfer tax rate for at least one year. In addition, a small group would like to see the estate tax repealed altogether. Some Democrats are happy to allow the transfer tax rules to revert back to the $1 million exemption amount and 55% top tax rate. The president and the Democrats aligned with him were seeking a middle-ground 45% top transfer tax rate and a $3.5 million exemption amount but, to reach an agreement before year end, may let the transfer tax resume its lower exemption amount and higher tax rate.

Comment

Advisers to international families may recall that the scheduled one-year repeal of the estate tax was not averted before its effective date of January 1 2010. It was not until December 2010 that the president and Congress reached agreement on the estate tax rules for 2010 (retroactively), 2011 and 2012. Once again the clock is winding down, making it difficult to advise multinational families with regard to succession planning. Nor can advisers provide complete solutions on organising a family's international holdings, given the uncertainty surrounding the implementation of the Foreign Account Tax Compliance Act. Most are working to complete large gifts prior to the end of the year in anticipation of a smaller transfer tax exemption amount in 2013. With the new year comes the hope that answers and guidance will be forthcoming.

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