



M A S E C O

Challenges facing US citizens living in the UK



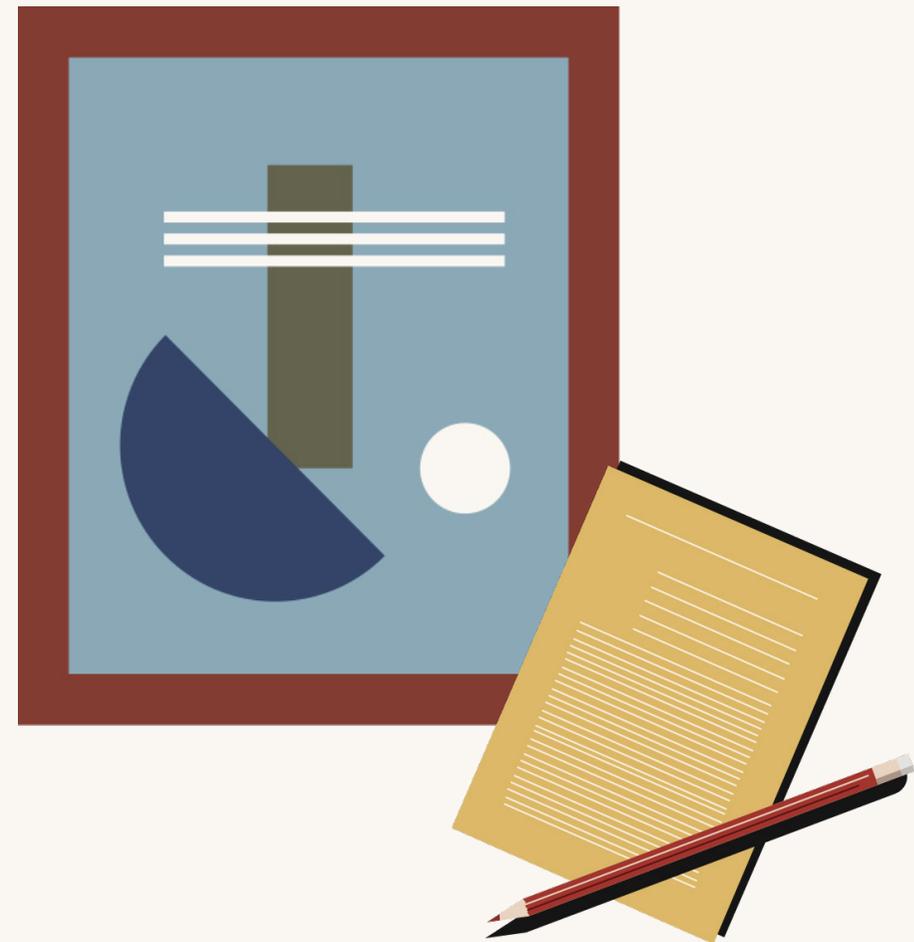
Challenges facing US citizens living in the UK

High net worth US citizens living in the UK face a number of complex challenges when it comes to allocating and investing their assets, from IRS and HMRC dual reporting requirements to conflicting tax considerations.

Rules and Regulations

Reporting obligations to the IRS and HMRC:

- The US taxes the worldwide income and capital gains of all US citizens regardless of where in the world they live.
- The US Bank Secrecy Act states that every US citizen, Green Card holder or resident must file a report of Foreign Bank and Financial Accounts (FBAR) if they have a financial interest in (or signatory authority over) foreign accounts worth \$10,000 or more during any one tax year. This includes US beneficiaries of foreign trusts.
- The passing of the Hiring Incentives to Restore Employment (HIRE) Act in the US and its Foreign Account Tax Compliance Act (FATCA) provisions were set up with the explicit aim of tackling offshore tax evasion. The Act requires all Foreign Financial Institutions (FFIs) to report all significant accounts held by US taxpayers to the US Internal Revenue Service (IRS).
- The UK's introduction of a 'stay-related' threshold (resident for seven of nine years) automatically attracts UK income tax residency status. UK resident non-domiciles have to pay either an annual levy to HM Revenue & Customs (HMRC) and continue paying tax on a remittance basis, or they must declare their income and gains on US (and offshore) assets and pay tax in the UK annually on an arising basis. Beginning in April 2017 anyone resident in the UK for 15 out of the last 20 years will no longer have a choice and will be required to pay tax on an arising basis. The vast majority of Americans living in the UK elect to pay tax on an arising basis anyway and are therefore taxed by the UK on their global portfolios.



Tax Issues

- Investing in UK or offshore ETFs, Unit Trusts and OEICs will cause them to fall foul of the IRS's Passive Foreign Investment Company (PFIC) rules.
- They will be taxed aggressively by the IRS and all gains may be subject to taxes and penalties of up to 100% of the growth in value of the investment.
- Utilising UK-based savings arrangements such as ISAs and SIPPs may have unattractive US tax consequences for US citizens resident in the UK. ISAs do not enjoy a tax deferred status in the eyes of the IRS and the US tax consequences of SIPPs are even more complex.
- The way the IRS classifies UK pensions is complex and beyond the scope of this paper. Most SIPPs would be classified in the US as 'foreign trusts'. As a 'foreign trust', growth within a SIPP is fully taxable. Fortunately, the UK has a treaty with the US that may allow the US taxpayer to claim the SIPP is a Foreign Pension and thus the growth in value will be tax deferred. This same provision may also protect the growth in company pension arrangements from becoming US taxable. Additional US trust reporting may arise for individuals. Many US citizens may consider using a QROPS as a potential pension structure. However, care should be taken as the transfer of assets from a UK pension to an offshore QROPS is usually considered a US taxable event, and the QROPS may also not be covered by the valuable treaty protection on any future growth in value.
- HMRC classifies the growth of most US Mutual Funds and Exchange Traded Funds (ETFs) as Offshore Income Gains (OIG) and the growth is taxed at the individual's marginal income tax rate rather than at capital gains tax rate. This is because the vast majority are Unregulated Collective Investment Schemes (UCIS) without reporting status. For most wealthy Americans, this would mean being taxed at up to 45% on all gains made on their portfolios. This can be exacerbated if the foreign exchange rate moves in an unfavourable direction. The net result is that there is a much larger gross UK tax liability for Americans who own US Mutual Funds or US based ETFs.



Investment consideration

It is essential to appreciate that Americans are taxed on a worldwide basis, irrespective of where income/gains arise.

Coupled with the past and upcoming changes to the domiciliary rules in the UK, this creates an additional set of challenges for US citizens living and working in the UK. Their investments need to be risk-managed, currency-sensitive and tax-compliant. An experienced investment adviser should also consider whether there are any tax-efficient or tax-planning opportunities.



There are a number of key considerations in developing an appropriate investment strategy and it is important that they are not looked at in isolation.

- Are any of the current investments US Mutual Funds and possibly taxed at income tax levels in the UK?
- Are any of the current investments PFICs for US purposes?
- Are the client's US education (529) plans structured appropriately for UK residents?
- Have appropriate tax wrappers been used to ensure that the currency of assets matches the client's long-term liabilities?
- Are the client's foreign tax credits being used effectively?
- In the case of couples who are of dual nationality, an understanding of the framework of both tax jurisdictions is vital.
- In the case of entrepreneurs, careful wealth structuring can result in flexible investment options.
- A deep understanding of legacy plans for US families can be of significant benefit when developing a wealth plan.

Getting good advice

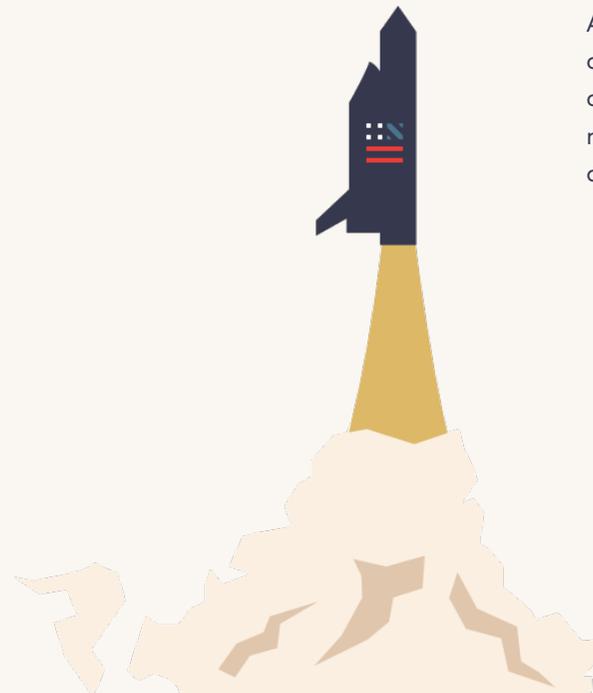
There are many reasons why Americans living in the UK should seek out the advice of an experienced wealth manager who understands their specialist circumstances and is authorised and regulated to give advice in the UK and the US. It is virtually impossible for investment advisers to adequately advise US citizens if they are not fully aware of the intricacies of US investment tax law, retirement planning and estate planning. MASECO is authorised and regulated by the Financial Conduct Authority (FCA) in the UK and by the Securities Exchange Commission (SEC) in the US. Its founding partners each have close to 15 years' experience specialising in this complex area.

Our Service

We provide an integrated wealth management service that encompasses the implementation and ongoing monitoring of US clients who need:

- Wealth structuring
- Investment strategy
- Tax-efficient investing
- Estate and Trust structuring
- Philanthropic considerations/Charitable Giving
- Relationship management

Although MASECO does not provide tax, legal or accounting services, we have a deep understanding of where they fit in the process. When required, we work closely with a network of expert US/UK tax advisers and lawyers. This professional network can help implement the complex tax and legal issues facing US citizens and we are happy to make appropriate introductions for you if required.





The MASECO solution

Portfolio management:

MASECO has developed market-leading strategies and structures specifically designed to cater to the needs of Americans overseas. Our portfolio management service includes managing assets within:

- Taxable Accounts
- SIPPS
- IRAs – including assistance with consolidating 401K plans
- ISAs
- Trusts
- Donor Advised Funds

US custody:

There are a number of reasons why it may be beneficial for Americans living abroad to invest globally but have their money custodied in the US:

- No FBAR – avoids up to 50% US tax penalties on filing mistakes on non-US based assets.
- 1099 US Tax reporting – makes life easier.
- Lower fees – custody and transaction costs are much lower in the US compared with most other places in the world.
- Tax-efficient accounts.
- US collective investments are typically much cheaper than offshore collective investments.
- If the custodian goes bankrupt clients are typically covered by \$500,000 SIPC (Securities Investor Protection Corporation) insurance and excess SIPC insurance.

- Custody is regulated by the SEC.
- Investments avoid coming under the IRS's Passive Foreign Investment Company (PFIC) rules.

US funds with UK reporting status:

- We generally invest our clients' assets in pooled funds that are subject to Capital Gains Tax treatment in the UK (28%) versus Offshore Income Gains of 45%. Clients may also use their annual CGT allowance against the growth in these funds.
- US tax-efficient and subject to 15-20% capital gains tax in the US, whereas PFICs can be taxed at up to 100% of the gain.
- The funds are tax managed from a US perspective with the purpose of reducing US taxes.
- We use institutional funds that are typically comparatively inexpensive.

Retirement accounts and planning:

- We help our clients make use of tax-advantaged retirement vehicles such as IRAs, 401ks and Roth IRA. This may help to reduce their tax burden.

Reporting and record keeping:

- Consolidated reporting in the UK and the US irrespective of where the assets are custodied. This allows for more accurate asset allocation and performance reporting.
- GBP tax year activity reporting.
- USD calendar year tax reporting.

MASECO Private Wealth is not regulated to provide tax advice either in the US or the UK. We strongly recommend that every client seeks their own tax advice prior to acting on any of the strategies described in this document.

MASECO LLP trading as MASECO Private Wealth.

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