AN INSIGHT TO US

EXPAT TAXES

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CHAPTER 1

Get Ready For Tax Returns

The US happens to be among the handful of countries across the globe that imposes taxes on their citizens based on their global income irrespective of where the earnings come from. This book is aimed at guiding you through all the complicated rules that are a part of US income tax return. You may consider this introduction to be a manual of sorts to the major areas of your US income tax return.

Prepare to Learn the Basics

It is a mandatory obligation for any citizen of the US to report his or her global income on your their IRS filings in the United States every single year, no matter where you are living. On the bright side, you will be offered three major opportunities for credits and deductions in a bid to do away with the problem of dual taxation.

Expatriates who are qualified for the foreign earned income exclusion can choose to exclude up to $95,100 from their wages earned abroad on their tax return in the United States for the year 2012.

The foreign tax credit allows a citizen of the US to be entitled to a credit on the foreign income taxes paid on their US income tax return.

The foreign housing exclusion provides taxpayers with the opportunity to subtract several housing costs exceeding certain amounts stipulated by country from their taxable income. In the end, depending on the cost of living for the country you are in, these deductions and credits can further minimize your taxable income if it is over the foreign earned income exclusion amount ($95,100)

Self-employed and Living Abroad...What then?

If you work for yourself, it gives you the chance to travel to any part of the world. However, you should know how this affects your US income tax return. Being a resident of the US, you are obligated to file for return on tax and provide details about your international income no matter where you live. Like any other self-employed person, you have to pay both the employer as well as the employee part of Medicare and Social Security taxes. Even if you happen to stay abroad, this responsibility may still be present. You should consider a few effective policies for tax planning which are likely to help lessen your US income tax liability.

In order to be qualified, a resident alien or US citizen needs to have earned their income abroad, and must face the test for physical presence or the test to determine bona fide residence.

You need to claim this exclusion on Form 2555. Attach it to Form 1040 before filing.
If you become eligible for the Foreign Earned Income Exclusion, you can also be eligible to deduct a part from the expenses of your housing, within a foreign nation, which is also covered by Form 2555.

Credit on Foreign Tax

The residence of a citizen of the US located abroad will probably lead to taxation in the particular country along with the US. The Credit on Foreign Tax has been devised in such a manner as to ease the load of double taxation, which is a perpetual cause of worry for the US Expats. Residents of the US can choose to claim some credit for international income taxes that have been charged on their US income tax return. The credit happens to be restricted to the sum of tax liability in the US stated as per Form 1040.

Foreign Bank Accounts

The Form 90-22.1 Report of Foreign Bank and Financial Accounts (FBAR) is due for filing by the 30th of June, every year, if you, regardless of being a taxpayer in the US, have economic control over international bank accounts and the combined total of these bank accounts crossed $10,000 any time throughout that calendar year. You need to file this form individually from your US income tax return and it needs to be received by the Treasury by the due date.

Non-US Resident as Partner

A citizen of the US can choose to file for a joint return along with their partners who are non-US citizens in case both the parties have agreed to consider the spouse as a US income tax filer for future years Although this election offers a lower tax rate as married filing jointly, (for income over the foreign income exclusion threshold), it also permits the US to levy taxes on the international income of the non-US partner. The election can go as planned only if an Individual Taxpayer Identification Number (ITIN) is applied for via the IRS using Form W-7. It is better to apply prior to filing your US income tax return since the usual time taken to process an ITIN application is six weeks.

Failure to Report Foreign Financial Accounts

The IRS is providing a chance to persons, who have not yet informed their foreign economic accounts, to become up-to-date on their US income tax return through August 31, 2011. This initiative seeks to offer a lesser penalty to individuals who have used up most of their compliance together with a "Get out of Jail for Free" card, effective against criminal prosecution.

Income Tax Filing Dates

April 15th is the date by which citizens of the US are needed to file all of their respective tax return as per US income. However, in case of a US resident living in a foreign country on April 15, that person is automatically given the right to some extra time for the purpose of filing their US income tax return until June 15. In spite of automatic extension benefits, you should pay all US income tax return by April 15 to prevent any interest or penalties.

Impact of Foreign Exchange

All the amounts, during the filing of your US income tax return, need to be informed in terms of US dollars. The IRS seems to accept a rate close to the average annual when different transactions are being made in spite of their preference that every transaction be changed to American dollars according to the daily rate. Selecting the correct method can result in a considerable amount of tax savings, based upon the fluctuation of the rates of foreign exchange. In some instances, however, making use of the rate that changes day-to-day yields greater tax savings on your US income tax return.

Extension...How to Get One?

You can avail an automatic extension for filing US income tax return just by affixing a declaration to your copy of Form 1040, while you file the form before June 15. Form 4868 can be filed to gain a further extension until October 15. If you require even more time to meet the test for physical presence or test to determine bona fide residency, you can ask for an extension by using Form 2350, which is normally granted until a period of 30 more days following the completion of either of the tests.

Dual Taxation

An arrangement has been reached by the US regarding treaties of tax with over 50 countries to prevent dual taxation of residents of US. In general, the treaties try to allocate the income of an individual simply to the cause of earnings.
IRS Publication 901 contains a lot of in-depth information regarding the provisions present in each of the treaties along with ways in which they can prove useful to you, in order to understand how the treaties affect your US income tax return.

Social Security

Advantages of Social Security are a part and parcel of being an Expat. The US has settled on agreements with a total of 24 countries to remove dual taxation as well as make sure that recipients are protected by Social Security facilities. Publication 05-10137 has been published by the Social Security Administration for the purpose of helping Expatriates take care of their benefits related to social security while they stay abroad. You can get information based on each nation on the Social Security website.

Taxes of the State

Every single one of the US states, fifty in number, utilizes a separate method to establish the requirements of filing of the US income tax return. A few states including Texas, Florida and Washington have no such individual income tax. Some states, on the other hand, like New Mexico, South Carolina, Virginia and California take into account the fact whether or not you have held on to some specific rights as a resident of the US like economic accounts, ownership of belongings and a driver's license so that they are able to get an idea about your long term intentions. If they get an idea that you plan to come back to that state later, they might still need of you to file for a return on tax.

CHAPTER 2

Role of a Global Tax Expert :

10 Reasons Why US Expats Need to Hire a Global Tax Professional

Reason 1 :
If you happen to be a citizen of the US or the holder of a Green card staying and working out of the country, you are bound by the conventions of the law to file for the US tax return every year.

If the IRS, by any chance, happens to uncover the fact that you have failed to file your tax returns as a US Expat, it could result in some serious trouble for you including spending time in jail or penalties.

Reason 2 :
You might have arranged your own taxes while you stayed in the United States; but be warned! It is better to hire an Expat specialist during the time you remain abroad due to the fact that this sort of tax return has a great deal more complexities and intricacies.

If you are an individual, and not an organization, living abroad, Form 1040 is required to be filed along with related schedules, in pretty much the same manner you are used to while living in the United States. However, there are specific schedule related to living abroad such as the Tax Credit for foreign taxes paid, the Foreign Earned Income Exclusion, the Foreign Housing Allowance or even the Foreign Housing Deduction. These documents might turn out to be too difficult to understand, but they happen to possess certain advantages that can lead to the saving of a considerable sum of money.

Reason 3 :
You should not make the mistake of confusing the tax year of your host country to the tax year in the US.

The US tax years starts from January 1 and continues right until December 31. But not all nations operate according to this timeframe. New Zealand, Australia, Hong Kong and the United Kingdom all have varied tax year phases.
The US insists on either you or else your tax preparer finishing your return as per the United States tax year, which requires you to obtain your tax reports from the country you are residing in for more than or equal to two years and dig out the proper facts, so that you can then apply them to your taxes as a US Expat. It may not be the most challenging task there is but it sure does take up a lot of your precious time.

Reason 4 :
Foreign Exchange Rates can turn out to be a real pain in the rear.

Learning about the official rates of Foreign Exchange and then changing the income you earn abroad into US currency may prove to be a rather lengthy activity. And if the year of your taxes does not happen to be similar to the tax year in the US, the process can take even longer. The majority of US Expats are likely to benefit greatly from having an expert handle all these conversions in order to make sure that no accidental mistakes are made. On top of that, you need to calculate the rates of exchange using different methods i.e. yearly, monthly and on certain days, to take care of the fact that you are changing at the rate most favorable for you and not the IRS.

Reason 5 :
An aggressive approach has been adopted by the IRS to ensure that tax returns are being filed properly by US Expats.

According to projections of the US Government, the US Treasury is deprived of almost as much as a huge sum of $100 billion per year due to offshore tax abuse. They are quite serious about tracking down the offenders and taking legal action against them. As soon as they manage to find an Expat that has not filed their taxes in the correct manner, very strict measures are taken to set the situation straight. This may result in property and bank accounts being seized, warrants for arrests being circulated, and a few US rights being stripped away with no prior notice. If you have fallen behind on filing your taxes in the US, you need to get in touch with the concerned authorities right away to improve the circumstances.

Reason 6 :
You are not likely to keep track of every single rule change that takes place from one particular tax year to the following one.

The tax codes in the United States are supposed to change each year, even more so when there have been some important alterations in the political office such as an alteration in Congress or the election of a new President. An Expat in the US can very easily miss one or even more of these restructured amendments, and in case the return happens to be audited, it can result in a number of penalties and civil fines. Most of the trouble stems from the fact that the administration does not normally take a break there, and if it is discovered that someone filed taxes improperly, then as a rule they audit the previous six years in order to locate any assets and other stuff that may not have been disclosed. This is sure to be a harrowing experience for any person.

Reason 7 :
A State return may need to be filed despite the fact that you have not resided inside the United States for the last couple of years.

There are a certain set of rules that each state maintains concerning Expats in the US, and in case of some states, these rules make it harder to get out of filing for a return. If it happened that you ever stayed in New Mexico, California, Virginia or South Carolina, you are still required to pay for a domicile tax in that particular state. You are able to claim a tax domicile if you possess a valid voter registration, property, bank accounts, driver's license or any other kind of assets that link you to the state.

Reason 8 :
Commercial software for tax purposes is not meant for use by US Expats and so you can miss any exclusions or deductions.

These programs have been designed primarily keeping in mind US citizens residing in the US, instead of a US Expatriate based in a foreign country. They have a higher chance of missing deductions and exclusions that can only be availed by Expats. An expert in taxes, proficient in international law, should have knowledge on each of the minor tax credits and rebates intended for your exact circumstance and make certain that you gain the correct credits and deductions.

Reason 9 :
Roping in an expert to organize your taxes is not necessarily an expensive matter.

Some of the better firms state their fees upfront so that you do not have to worry about any kind of hidden costs. Moreover, the flat rate charged by them to get the Federal tax return ready for you is not at all astronomical. These firms are well aware of the workings of international law and the way in which it is applicable for Expats in the US. Therefore, they are able to arrange your return as swiftly as possible in a way that is professional and will probably end up saving you both money as well as time in the end.

Reason 10 :
Last, but not the least, the best explanation why you need to rope in a worldwide tax professional to prepare your taxes as a US Expat for you this year!

The thought of sitting cooped up inside your home for long periods, trying to sort through all your taxes is not a pleasant one. There can be about a hundred different things that can go wrong. For all you know, the forms and schedules that you are required to file could change. Missing even a single one of them

might bring about dire consequences with the United States Administration. Most international tax practitioners know what they are doing from years of experience and all take pride in the fact that they complete for Expatriates in the US. You simply need to go out, enjoy life and leave all your income tax worries to the professionals.

CHAPTER 3

How to Determine If You Are a US Expat

You are required to pass either the Test for Physical Presence or the Test of Residence for a Bona Fide citizen to be considered a US Expat

Test to Determine Physical Presence

The Test for Physical Presence has been devised in such a way as to provide US Expats with a tax exclusion for those individuals who have stayed abroad, only on a temporary basis, for a period equal to or greater than eleven months. If you manage to get qualified for this exclusion, you can considerably diminish or altogether remove any benefits of being a US Expat in the course of a calendar year. However, you need to know that this policy comes with its fair share of pitfalls. The best way to make sure that you become eligible for the Test for Physical Presence is to consult a tax expert.

Qualifications

You need to first meet a few specific criteria before you can meet the conditions of the Test for Physical Presence.

- *You should be a citizen of the US or a resident alien*
- *You need to be present away from the United States for a period of 330 days out of any consecutive 365 day phase*
- *Claiming status from North Korea, Cuba, etc. will not work; you need to be within a foreign nation legally*

Additional Factors

Each day spent on United States soil, including within US territories, happens to be taken away from the overall period. Plus, every day you spend going away from or towards the US is also subtracted. US Expats are able to receive several exclusions and tax credits, such as the Tax Credit for foreign taxes paid, the Credit for Housing in a Foreign Country and the Foreign Earned Income Exclusion, under the Test for Physical Presence. You simply need to remember to stay somewhere else other than the United States for a minimum of 330 days out of the total time span comprising of 365 days. This particular period of time, instead of being determined according to the ongoing calendar year, takes into account past 12 months for the benefit of calculation. You need to keep in mind that no matter when a US Expatriate makes an entry US soil, an entire day is subtracted from the time they spent overseas.

Important Points

The Test for Physical Presence is applicable to any successive phase comprising of 365 days and it might begin on any random day of any given month

- *The Test for Physical Presence is not affected by any exclusionary causes.*
- *This indicates that if you remain on United States soil, no matter what the reason (work, vacation, sickness, etc.), it is considered to be opposed to Expat of the US*
- *Any form of worldwide travel that results in a US Expatriate being brought brings onto US soil is regarded as a disqualifying day since that individual is no more inside a foreign nation*
- *If you earn any income inside the US while the 365-day calculation phase is still going on, you might end up facing tax liability to the IRS in spite of having met the requirements of the Test for Physical Presence.*

Residence Test for a Bona Fide citizen

The Test of Residence for a Bona Fide citizen happens to be a process used on taxes of US Expatriates to establish whether or not a person meets the eligibility criteria for particular tax deductions. This test comes with a few simple criteria that can be utilized by your tax preparer to verify your eligibility. Like everything associated with the IRS, there may be exceptions which you need to confirm before taking for granted that you will meet the conditions and you may require some further help in completing Form 1116 or Form 2555 for the IRS since it can be quite complicated.

Qualifications

There are four specific criteria, which you need to meet prior to being considered a bona fide citizen on your Expatriate tax returns.

- *Be a resident alien or US citizen*
- *You need to possess an established home overseas*
- *You are required to stay within the foreign residence for the whole calendar year*
- *Plan to stay inside the foreign country for an indefinite period of time In order to be eligible for the Test of Residence for a Bona Fide citizen, an individual needs to live abroad for the entire year, without any immediate aim of returning to the US on a permanent basis. The second half of the stipulation may lead to some tax concerns for US Expats.*

What you need to understand

A Bona Fide citizen status can have an intense effect on your Expatriate tax returns and can even help save thousands of dollars. The IRS normally supervises each claim on a case by case basis owing to a greater part of the Test of Residence for a Bona Fide citizen being rooted in future plans. Some circumstances might prove to be too difficult to interpret while filing your tax return as a US Expat, in which case, it might be a good idea to speak with an Expat tax professional before submitting your taxes and obtaining these exemptions.

Three Major Features of Foreign Taxes

US Expats who only want to work abroad can find the laws concerning international taxation to be rather tricky. Several different laws must be taken into account and most of the foreign countries have different policies relating to residency, Social Security, international capital gains, among others, that are often at a risk of going unnoticed. It is a no-brainer that a skilled international tax accountant needs to be spoken to before taking on employment in any foreign nation. However, there are three things in particular that every US Expatriate needs to commit to memory when it comes to shelling out foreign taxes.

Residency Normally influences Where Taxes are Due

No matter which part of the globe your income comes from, being a citizen of the US, you will at all times be expected to file a regular 1040 tax return. The sole point of difference earning income abroad has on this particular situation is where taxes will, in fact, be paid to, and it differs to a large extent depending on the country and their residency laws. Countries like Brazil, United Kingdom and France deem any person who has stayed within the country for over 183 days to be a resident, while other nations stick to a totally different set of guiding principles. Some countries, including Japan, collect taxes from non-residents as soon as employment is confirmed, so it is always advisable to look into these laws previous to assuming residence outside the United States.

Not Every Nation Goes by the Calendar Year for Tax Reasons

Australia sets their tax year on income received from July 1 to June 30 the next year while the United Kingdom uses April 6 to April 5. It is not hard for a US Expat to take a trip to a different area and fail to notice these variations in when they are meant to file. If by chance taxes are not paid as a result of a confusion in dates, the sentence can often be somewhat harsh. The US expects taxpayers to file a 1040 on income from the financial calendar year no matter what the filing conditions of another country are. The returns are normally due by 15 June, but exceptions occur from time to time.

Double Taxation...It's a Real Thing

A lot of US Expats take for granted that simply because they are paying taxes in one region, they are necessarily excepted from paying them once more within the United States. This may be true to some extent in certain cases, but you are not likely to get any benefit until you file a Form 1116 and Form 2555, which apply for tax credits, the foreign income exclusion as well as overseas housing exclusions. In addition, US taxpayers have to claim factors such as accumulated interest on investments. The process does not seem to be automatic, and the IRS can and will track down unpaid taxes when they have not been reported in the correct manner. The IRS may go so as far as to file criminal charges against the US Expat if the government has reason to believe that the citizen evaded his tax liability on purpose.

Foreign Earned Income Exclusion, Tax Credit for Foreign Taxes Paid and Foreign Housing Expense

Foreign Earned Income Exclusion

The Foreign Earned Income exclusion is basically a string of tax credits for workers who are living overseas. These are reported on Form 2555 and are meant to be filed along with your Form 1040. Being a US Expat, all of your income is subject to the same rate of tax that workers within the US are liable for. However, you can make use of stipulations like the Tax Credit for Foreign Taxes Paid and Foreign Earned Income Exclusion to diminish your tax returns of a US Expat. The Foreign Earned Income Exclusion offers you the opportunity to slash up to a hefty amount of $95,100 of your foreign earned income on your Expat taxes. Moreover, given that you will probably be paying for expenses such as housing and living costs while you earn your income in a foreign country, you may also be capable of removing some of these costs. This credit can compensate for a part or even the whole of your tax responsibility as a US Expat if you meet some basic requirements.

The Test of Residence

US Expats are required to meet at least one of two criteria in order for them to qualify for the Foreign Earned Income Exclusion.

- *You are required to find some full time work within a foreign nation for the duration of the whole calendar year, also called the Test of Residence for a Bona Fide citizen.*
- *Work in a foreign country for a minimum 330 days out of any extended period of 365 days, known as the Test for Physical Presence.*

While both these stipulations may seem somewhat alike, in reality, they are greatly varied as regards the manner in which they would affect your taxes as a US Expatriate. US Expats are automatically qualified for this exclusion if some of their time has been spent working abroad right through the whole calendar year which extends from the 1st of January till the 31st of December. After that, they are deemed a bona fide citizen. The second statement may appear to be a bit confusing at the time of relating it to your Expatriate tax return. This clause basically entails that an individual left the US for business purposes but has refused to come back for over 35 days in the course of the previous twelve months. It is important to mention that no reference has been made to consecutive days which implies that a Expatriate from the US would become disqualified if he undertook numerous short outings to return to the United States that added up to over 35 days in the course of the 12 month span. The solution to acing the Test for Physical Presence is to have stayed below 35 days within the United States for a period consisting of 12 months.

Exemptions

If an individual manages to meet any one of the two conditions specified, then they are permitted to take away up to $95,100 of the income they earned abroad from their Expat taxes in the US. If you happen to be married and are filing together, you will be able to remove up to an amount of $190,200 from your tax returns as an Expat for the tax year 2012. The sum is filed for inflation as well and increases every year. You would also be eligible for the Foreign Housing

Allowance.

True to its name, the Foreign Earned Income Exclusion depends only on the income earned from overseas for the purpose of calculation and the earnings needs to be worked for. Foreign earnings gained from sources like interest, dividends as well as rental earnings is not taken into consideration since, as far as the IRS is concerned, this income does not seem to be earned. Furthermore, US-based income from sources like pensions will also not be eligible for this omission, as the earnings were not gained from within a foreign land.

Ordinary Troubles

Foreign Earned Income Exclusion is usually accompanied by some loopholes and problems. Therefore, it is best to have a discussion with an international tax professional regarding your particular situation. Expats can be taxed inside the US under some circumstances even if they happen to be a resident of a foreign nation and have worked well below 35 days inside the United States. Not all US Expats are able to make the most of the Foreign Earned Income Exclusion. If you happen to be an employee of the US Government and are paid by the

United States Government, then you are in a position to use the Foreign Earned Income Exclusion to reduce your tax returns as a US Expat.

Tax Credit for Foreign Taxes Paid - Form 1116

You may have to face dual taxation if you move overseas. However, the IRS permits a US taxpayer to draw a credit on his US Expatriate tax return for any foreign taxes imposed. This benefit helps you decrease your US tax responsibility and save you money on your US Expatriate tax return. Form 1116 is used to claim the Tax Credit for Foreign Native, which is filed together with Form 1040.

Limitations

The Tax Credit for Foreign Taxes Paid stated on your Expatriate tax return can never surpass the amount of US tax you shell out on foreign income. The total earnings generated overseas, rental income from foreign assets and dividends obtained from foreign companies should all be included within foreign source taxable income. Any subtractions directly associated with these earnings maintained on the tax return needs to be eliminated prior to reaching the ultimate taxable income. Income earned both within and outside the United States needs to be assigned according to the period of days worked within the United States and the number of days worked overseas.

Qualifications

You need to meet with four criteria in order to obtain the Tax Credit for Foreign Taxes Paid in your Expat tax return.

- *The tax should be evaluated on income*
- *You need to have a tax responsibility that has either been compensated or incurred.*
- *The tax needs to be imposed on you as an individual.*
- *The tax needs to have originated legally in a foreign nation.*

You can claim the Tax Credit for Foreign Taxes Paid on an annual basis by finishing Form 1116 and attaching it to your Expatriate tax return. The credit decreases the liability of US tax dollar-for-dollar. All foreign taxes paid in US dollars need to be reported. The IRS expects each deal to be changed at the foreign exchange rate on the date of transaction.

Challenges

Certain kinds of foreign taxes are ineligible for the Tax Credit for Foreign Taxes Paid. These comprise of taxes offered to a few particular nations like North Korea, Cuba and Iran. You are not able to claim a handful of taxes on your Expatriate tax return including dividends that are derived from each company owned 10 percent to 50 percent by foreign countries, financial services income, shipping and domestic income, dividends from foreign sales corporations, domestic global sales company dividends, foreign oil and gas extraction income and income on foreign transactions from overseas sales companies. You cannot take a credit for these costs on your Expatriate tax return, but can claim them through Schedule A as an itemized subtraction.

Carryforwards and Carrybacks

If your Tax Credit for Foreign Taxes Paid happens to be larger than the US income tax responsibility worked out on your Expatriate tax return, it is possible to carry back the credit to the tax year previous to the present, or you may choose to carry it over during the course of the following ten years. You can make use of the extra credit in order to get some sort of refund out of the year before, or elect to offset the tax liability of your future years on your foreign earned income.

A Matter of Choice

The foreign taxes you paid for this year can affect your Expatriate tax return in a positive manner in two different ways. The first method, which also happens to be the most favorable, is to complete Form 1116 and avail the Tax Credit for Foreign Taxes Paid on your taxes as a US Expat. The other option is to take the taxes as an itemized deduction on your Schedule A. The credit is usually the more worthwhile choice since it offsets your tax responsibility dollar for dollar. Additionally, you may elect to take the credit in spite of not itemizing your deductions. But considering the foreign taxes to be a deduction decreases the amount of income that is taxed and is likely to result in a greater tax liability on your Expatriate tax return.

Foreign Housing Expense

A citizen of the US living overseas is able to remove some of his housing expenses from the net income, known as the Foreign Housing Allowance. The IRS takes into account the fact that the cost of housing out of the US differs from the housing expenses required within the United States. You may be required to spend a greater amount of money on housing, which could have a negative impact on you in terms of finances. So, the IRS presents you with a deduction, which is equal to a part of your foreign housing costs, based on your area of

residence and the number of days you have spent away from the United States. In order to be eligible, you first need to meet the terms of the Test for Physical Presence or the Test of Residence for a Bona Fide citizen.

Working Mechanism

The Foreign Earned Income Exclusion limits determine the sum of money you can deduct from your housing expenses. For the tax year of 2012, the Foreign Earned Income Exclusion seems to be $95,100. You can choose to deduct up to 30% of this as part of your Foreign Housing Allowance. Therefore, you are permitted to deduct a maximum of $27,450 every year from your housing costs. Expenses like domestic labor costs, furniture, mortgage payments, etc. do not qualify. In case of any doubt, you need to get in touch with your tax preparer. You need to keep in mind that the IRS sets the maximum limitation based on geographic variations in housing expenses, relative to the cost of housing in the United States. In order to calculate the amount you can deduct, you first need to come up with your base amount, which happens to be the least non-deductible sum of your housing that you are required to pay for. For the year 2010, this is calculated as being 16% of the maximum Foreign Earned Income Exclusion.

CHAPTER 4

State Filing Information for US Expats

States which are Conducive to Tax Returns for US Expats

Out of all the fifty states present in the United States, nine of them offer conditions, which are favorable for the purpose of tax returns of US Expats. The states of Nevada, Texas, Florida, South Dakota, Wyoming and Washington have no sort of taxes related to state income. Basically, this indicates that there happens to be almost nothing, which they will try and attempt to collect during the time you are earning wages in a foreign country. Tennessee and New Hampshire fall in the list of states that are deemed favorable for reasons related to tax returns from US Expats since they collect taxes only on interest and dividend income.
If you are a resident of any of the nine states stated above, you are able to work in a foreign nation without facing any kind of trouble regarding the acquirement of a tax bill from the state that has been generated off of your Federal Expat tax return. It would be better if you are able to relocate to any one of these more favorable states prior to going abroad to work since no particular individual taxes on income are claimed in these parts. This could result in your saving a lot of money by preventing taxation by the state and not being required to necessarily file a tax return to the state at the time of filing a tax return as a United States Expat.

States which are Not Favorable for Tax Returns of US Expats

In case you, as a US citizen, happen to have residency in Virginia, California, New Mexico or South Carolina, chances are you will face a much more difficult time shedding your residency status and will, therefore, probably need to add in a tax return to the state along with your tax return as an Expatriate. Every single one of the governments considers their taxpayers to be an asset to the state and they are never prepared to relinquish control over that without some sort of fight. The downside to this kind of view is that you are supposed to shoulder the weight of the proof to show the administration that you are not going to be living inside that jurisdiction any longer and, as a result, should not be expected to file a state return with your tax return of US Expat. If you intend to return to any of these states in the form of a resident sometime in the coming years, it may turn out to be quite difficult to establish that no longer so you have the status of an actual citizen.

The states of South Carolina and California, in particular, are very thorough in tracking down any sort of connections that a Expatriate of the US still shares with their previous community, using a number of different methods as proof of residency. You probably need to file Expat tax returns in these US states lest you happen to have:

- *Telephone and utility bills*
- *Mail correspondence*
- *Dependents residing inside the state*
- *Lease payments or mortgage on property*
- *Voter registrations*
- *Association memberships*
- *Hold a state driver's license*
- *Library cards*
- *Have State bank investments or accounts*

If you want to effectively cease your status as a citizen with these states, a good number or even every single one of the ties given will need to be substituted with another permanent address within a different region or state. You will at all times need to shell out taxes on employment or rental earnings generated from inside these states, irrespective of the fact whether you still remain a citizen or not. This would require to be carried out on your tax returns of the State.

States that Remain Neutral

The situation is neither advantageous nor very complex for United States Expat taxes in the rest of the thirty-seven US states. The majority of these US states will deem you to be an ex-resident if you remain out of the region for a minimum of six months provided that you can offer proof of citizenship somewhere else.

CHAPTER 5

Self-Employment Expat Taxes

Introduction

You are free to move about anywhere in the world when you work for yourself. But it is important to know what kind of an impact this decision will have on your US taxes. Being a citizen of the US, you are required to file a tax return and report your international income, no matter where you reside. You need to pay both the employer and employee half of Social Security and Medicare taxes as a self-employed person. Even if you live in a foreign country, this obligation is still present. But there are a number of effective tax planning policies that allow you to decrease your US income tax return.

Self-Employment Concerns

Tax Issues Affecting Self-Employed US Citizens Working Overseas

If you happen to be self-employed in a foreign nation, your US income tax return might turn out to be somewhat more difficult, regardless of the fact whether you own your own corporation or are an independent contractor. A self-employed person is required to pay self-employment taxes on their own behalf due to the absence of any employer to do it for them. The housing exclusions and foreign earned income will offset the income earned through self-employment, but it will not be able to offset the extra 15.3% self-employment tax levied against the earnings. If you have not filed your taxes in a while, it could mean higher interest and penalties assessed on back US income tax return than if you were employed in a foreign company.

Think Positive!

The US has entered into treaties with a number of countries that possess their own social security equivalent strategies. If you work and live overseas, you may be required to pay into the foreign country's social security program. You will not have to shell out US self-employment tax on your income if the US happens to have an agreement with the country you stay and work in. This will allow you to save some money on your US income tax return. Countries like United Kingdom, Germany, Australia and Canada, all have agreements with the United States. The taxpayers usually have to carry out some amount of legwork, in spite of the presence of these agreements, to confirm their involvement in the social security program of the country, like acquiring certificates of coverage.

Social Security Taxes and Foreign Earned Income Exclusion

The majority of US Expats living and working overseas depend on the Foreign Earned Income Exclusion or FEIE to decrease their foreign earned income by $95,100 for the year of the US income tax return i.e. 2012. This exclusion can be made use of to offset self-employment income and is adjusted according to the expenses of your business. The only noticeable drawback is that the exclusion cannot be used to decrease the calculation of self-employment taxes.

Medicare and Social Security taxes account for 7.5% of the income earned by any US employee of a company, while the employers compensate a further 7.65% on their behalf. But, being a self-employed person, you need to pay both sides that come to a total of 13.3% in self-employment taxes in 2012. This money should be paid before the FEIE, which implies that there is an actual out of pocket cost here. You can, however, offset this expense if you happen to be paying the Social Security equivalent in a foreign nation and there exists a Totalization pact between your country of residence and the US. Additionally, the FEIE is prorated depending on the sum of expenses allocable to your self-employment trade.

The Foreign Earned Income Exclusion, as worked out on your US taxes, will be decreased in proportion to your business costs. Forty percent of your earnings went towards reducing your net income, thereby even lowering your FEIE by 40%. You can use the Foreign Tax Credit to reduce or altogether eliminate your US tax load, supposing you are paying taxes in a foreign nation on your self employment earnings.

Totalization Agreements

Your residence and self-employment income may lead to a tax responsibility in a foreign social security program in a few countries. The United States has entered into Totalization Agreements with a total of 24 nations in order to remove the dual social security taxation of citizens of the US. You can get further information on Totalization Agreements and the way in which they can help your US income tax return from the Social Security Administration. You will probably be able to verify the fact that you are excused from paying US social security taxes by offering a certificate of coverage from any one of the foreign countries under the Totalization Agreement.

Business Structuring Policies

You need to determine your business as its own entity if you want to evade hefty self-employment taxation. Out of so many different business structures, it is necessary to know which one to opt for. Sole proprietorships, partnerships and limited liabilities companies (LLCs) are considered to be pass-through entities

since the income or loss of the business is directly shifted to the individual owner's Expatriate tax return and there is no Expat tax payable from the business itself. You may be able to set a limit on your personal liability by setting up one of these businesses, but you will still need to pay the self-employment taxes on your gross income.

You could also try arranging your business as a C Corporation. Since a C Corporation is not a pass through entity, any profits maintained by a C Corporation will be taxed via the corporation. If you establish yourself as a staff of the corporation, you have the option to pay yourself a salary that is stated as wage income on your US income tax return. The salaries and related payroll taxes paid to you by the business will be a deductable business cost and will lessen your total tax responsibility. But C Corporations can be quite difficult to launch and come with tough reporting conditions, which leads many Expats to consider the next best option – S Corporations. An S Corporation is more or less like a partnership as the corporation itself does not have to pay any taxes, but the entire profit is passed through to the shareholders in order to be reported on their own US income tax return. Shareholders who offer their services to the S Corporation need to pay themselves a sound salary. The company pays the employer part of payroll taxes that comes to 7.65% and the recipient has to come up with the employee portion, which is also equal to 7.65%. Any income, which is not paid to the shareholders as salary, will be deemed a shareholder distribution, and taxed as normal earnings to the shareholder. The IRS has put some strict rules in place regarding the practical compensation of S Corporation shareholders since taxpayers have taken advantage of the situation more than once by understating their wages on their US income tax return. You need to make sure that you pay yourself the current market rate for your services, and take into account the time spent and level of skill required.

Another effective planning tactic for US income tax return is to regard your partner as a staff of the company. You will get double the Foreign Earned Income Exclusion when you file a joint return on US income tax return. Moreover, if you have been successful in establishing yourself as a corporation, you have the chance to receive double the wage payments.

Foreign Corporations vs. Entities

Every single business structure seems to have some sort of effect on your US income tax return along with its very own collection of benefits and difficulties. Setting up your business overseas come with advantages, especially if you opt to register your business in a region favorable for taxes. Tax heavens comprise of United Arab Emirates, Nauru, Monaco, Andorra, Norfolk Island, Cayman Islands and Nauru.

If you establish yourself as being a kind of C Corporation, registering your business overseas with no such income tax, you have the opportunity to remove your global tax responsibility. Simply offering yourself a wage lower than or as same as the Foreign Earned Income Exclusion, you will get a chance to remove your individual responsibility for US income tax return. The company will not have to shell out Medicare or Social Security taxes for your part and the taxable US earnings you had will be eliminated along with the FEIE too.

However, when you sign your business up in the United States, it comes with some benefits too. A business that is based in the US will be qualified to allow its most of its staff to venture in some domestic staff pension policy or even IRA. There are some advantages from the US income tax return that crop up from investing in local retirement policies. If you are an Expat that plans to retire inside the United States, you may want to keep this option open.

Furthermore, businesses that are based in the US will be in a better position to make the most of tax benefits related to property investments. A lot of people invest in real estate since the related deductions permissible against the property comprise of depreciation on buildings, mortgage interest and maintenance costs associated with upkeep. Another great reason for investing in real estate is because it gives you the capacity to take advantage of a like-kind swap, which permits you to invest 100% of the profits from the sale of a particular property into another without any kind of capital gains tax allegations.

CHAPTER 6

Tax Suggestions for US Expats Multicultural Family

Before you start with the process of prepping taxes for US Expatriates, you will most probably have a lot of questions in your mind, especially so if you happen to be married to someone who is not a resident of the United States and your kids belong to multiple nationalities.

The most common doubts are:

- *Will you be able to file together with your spouse who is a foreigner?*
- *Do you have the ability to claim children who were born outside of the United States as dependents*
- *In what way will this process affect the application for your partner's green card?*

Coming up with the answer to all these questions is sure to prove beneficial for any multicultural family.

Status of Filing

Even before you start the process of organizing your taxes as a US Expat, your first priority should be to establish the status of your filing that will turn out to be helpful to your circumstances. For purposes related to income tax in the US, the status of your marriage on the final day of a calendar year is considered to be the whole year's marital status. Being a citizen of the United States, married to some foreigner, you are provided with three different options for the status of filing – married filing together, married filing separately, and head of household.

Head of Household

In case there is a dependent in your family and you happen to be unmarried, you are able to file in the role of Head of Household. If you opt for this status of filing, it can give you subtraction that is more standard as well as comparatively lower rates of tax. However, if you have gotten married, you are able to claim the status of Head of Household only if got separated in an official manner or have remained apart from each other for the minimum duration of the latter half of that year.

Married Filing Separately

If your partner happens to earn a large amount of income, it would be better for your tax expert on US Expatriates to choose the Married Filing Separately option. In case you file taxes individually, no tax is levied on the income of your spouse in the United States. If your source of income is overseas investments or rental properties, it may be more useful from the viewpoint of the preparation of taxes for US Expats to assign these earnings to your partner and file individually. This would allow the income to not be subjected under the tax laws of the United States. The only limitation to this strategy of tax planning happens to be the tax laws related to community property in the United States. The income earned will be deemed to be the partner's income that carried out the job, or took control of the transactions.

Married Filing Jointly

If a non-resident of the US happens to be your spouse, you can choose to file together with your spouse who is a foreigner, by affixing a declaration to your tax return for US Expats. By agreeing to this election, the opportunity to permit the imposition of taxes on the earnings of your foreign spouse inside the United States for the present as well as the future is gained by you. If you become qualified for this election, you can double the amount of Foreign Earned Income Exclusions you get. In case of the tax year of 2010, this would indicate an increase in the sum of the Foreign Earned Income Exclusion from just $95,100 for only one individual to a hefty $190,200 for the couple as a whole. You need to remember that in order to file together, your partner is required to acquire an ITIN or Individual Tax Identification Number, which is provided by finishing Form W7, followed by submitting it to the IRS. This application takes a period of at least six weeks to be processed. So, you need to make sure that you submit it early in order to meet the deadlines of tax filing. The decision to file together with your foreign partner continues for an indefinite period, unless some sort of revocation is carried out by any half of the couple or death. In case of revocation of the election, it is not possible to get it elected by the very same individuals ever again.

Matter of Dependents

Residents of the United States are able to claim exclusions for their dependents if you meet the following five criteria:

- *The dependent needs to be a resident or citizen of the United States.*
- *He or she should be a part of your residence or even a relative.*
- *The dependent must make lesser wages than the exemption amount for the present year.*

- *Should be unmarried.*
- *You need to come up with over half what is required to support them.*

If a child has been conceived with your foreign partner, you are usually able to claim this kid on the return of your taxes (filing separately or jointly) in case that child happens to be a resident of the United States or a citizen for a portion of the current tax year. You should bear in mind that only a single spouse is allowed to claim the kid on their taxes as US Expatriates.

If you would have opted to file individually with your spouse having no source of earnings, you would have been able to claim some kind of exclusion for your foreign spouse if they met the same conditions established above. An ITIN or social security number is required for every single dependent being claimed on your tax return. The IRS is likely to automatically deny the claim of exemption without this.

Impact of Green Card

If your spouse, who is not a resident of the United States, has submitted or means to submit an application for green card, the best bet would be to take the decision to file together with you along with permitting their earnings to be taxed inside the United States. The administration of the US finds your proactive income details quite favorable, which increases the possibility of obtaining a green card. As soon as the green card is acquired, following the laws of filing taxes in the United States is a must. So be sure to try and meet that term beforehand. In case you have failed to file your taxes as a US Expat properly and now want to submit an application to get a green card, which is meant for your partner, it is advisable to be up-to-date on your taxes in the US before applying. Otherwise, it might result in your application being rejected. Be sure to first get in touch with your regional Embassy regarding the number of returns they suggest you file since this depends from one nation to another.

Compliance in Taxes

What happens if you come to know through some research that you did not file your taxes or, even worse, filed them incorrectly? There is no need to panic since it is simple enough to become compliant with your taxes as a US Expatriate. The only attributes you need to possess are patience, a skilled preparer and the proper documentation. Furthermore, new IRS guidance has clarified the expectations for someone who is living abroad not filed their taxes, it is mandatory that they file for the previous 3 years.