Short Taxes
United States 2020

Investment basics:

Currency – US Dollar (USD)

Foreign exchange control – While there are no general restrictions on remittances of profits, dividends, interest, royalties or fees to nonresidents, sanctions and embargoes apply to listed countries and entities, with restrictions on foreign payments, remittances and other types of contracts and trade transactions. Regulations are prescribed by the US Treasury and the Treasury's Office of Foreign Assets Control maintains related lists. Extensive currency transaction reporting and recordkeeping requirements also apply.

Accounting principles/financial statements – The US Securities and Exchange Commission requires publicly traded companies to file their financial statements according to US GAAP, which is set by the Financial Accounting Standards Board (a nongovernmental entity) for public and private companies and nonprofits.

Principal business entities – These are the corporation, limited liability company, business trust, partnership and limited partnership, usually created under the laws of one of the 50 states or the District of Columbia. US business also may be carried on directly by an individual (sole proprietorship) or a US branch of a foreign business entity.

Corporate taxation:

Residence – A corporation (or partnership) is "domestic" for federal tax law purposes if it is created or organized in the US or under the laws of the US, one of the 50 states or the District of Columbia. If certain transactions are executed whereby a foreign corporation directly or indirectly acquires substantially all of the property held directly or indirectly by a domestic corporation (or substantially all of the property constituting a trade or business of a domestic partnership) (an "inversion"), the foreign corporation may, in certain cases, be treated as a domestic corporation for purposes of applying US tax provisions.

Basis – Domestic corporations are taxed by the federal government on worldwide income, including income from branches, whether or not repatriated. Profits of foreign subsidiaries usually are not taxed until they are repatriated as dividends, unless they are subject to current inclusion under the "subpart F" (see "Controlled foreign companies" below) or passive foreign investment company (PFIC) qualified electing fund rules. A foreign corporation is taxable on income effectively connected with the conduct of a trade or business in the US ("effectively connected income" or "ECI") and on most non-ECI that is derived from US sources (see below under "Taxable income"). A US trade or business (e.g.a business conducted through a branch office located in the US) is relevant for this purpose if conducted by the corporation, by a partnership in which it is a partner or by a trust or estate of which it is a beneficiary.

Taxable income – Domestic corporations are taxed on nearly all gross income (including, e.g. income from a business, compensation for services, dividends, interest, royalties, rents, fees and commissions, gains from dealings in property and income from a partnership), from whatever source derived, less allowable deductions for depreciation, amortization, expenses, losses and certain other items.

A foreign corporation is subject to this same tax, except that taxable income for this purpose is limited to the gross amount of its ECI, less deductions allocated thereto. Two types of income generally deemed to be ECI in all cases are net gains from sales of US real property interests and, in the case of a foreign corporation treated as engaged in a US trade or business, gains from the sale in the US of inventory or certain other noncapital assets.

A tax treaty may eliminate the income tax on a foreign corporation's ECI, except to the extent such income is attributable to a permanent establishment (PE) in the US.

Unlike a domestic corporation, a foreign corporation that earns ECI also is subject to the "branch profits tax," equal to 30% (or a lower tax treaty rate) of the corporation's earnings attributable to ECI that do not remain, or become, invested in the US trade or business. If a foreign corporation deducts interest in computing ECI and the deduction exceeds the US-source interest paid by the corporation, the corporation also must pay a tax equal to the excess times 30% (or a lower treaty rate that would be applicable to US-source interest income from a domestic subsidiary).

In addition, and also subject to tax treaty-based reductions, the US imposes a 30% tax on the gross amount of a foreign corporation's

US-source non-ECI (e.g. dividends, interest, rents and royalties) other than certain property gains (see below under "Withholding tax").

Taxation of dividends – A dividends received deduction is available for dividends received by a corporate shareholder from a domestic corporation, at a rate of 70% (for a less-than 20% shareholder), 80% (for a noncontrolling shareholder owning 20% or more) or 100% (for distributions among members of the same affiliated group, provided other requirements are met).

Capital gains – Gains recognized by domestic corporations on capital assets (e.g. assets held for investment) are taxed at the same rate as ordinary income. Capital losses may be deducted against capital gains, but not against ordinary income. Relief from gain recognition is available for sales or exchanges of business assets in certain situations. A foreign corporation generally is exempt from tax on capital gains, unless the gain is from the sale of a US real property interest or is connected with the operation of a US trade or business tax on the latter may be eliminated under a tax treaty in certain cases).

Losses – A corporation's net operating losses generally may be carried back two years and forward 20 years.

Rate – A flat tax of 35% applies to the taxable income of a corporation that has taxable income for the year equal to or greater than USD 18,333,333. Graduated rates, starting as low as 15%, apply to income of a corporation with total taxable income of less than USD 18,333,333. The gradations in the rate brackets that apply to a single corporation's progressive amounts of income phase out as the corporation's total taxable income rises from USD 100,000 to USD 18,333,333. For this purpose, members of a controlled group of corporations are treated similarly to a single corporation.

Surtax – No

Alternative minimum tax – Domestic and foreign corporations are liable for a 20% alternative minimum tax (AMT) to the extent 20% of an adjusted measurement of income, computed without certain preferences, exceeds the regular tax on taxable income.

Foreign tax credit – Foreign income taxes may offset dollar for dollar the US income tax on taxable income, to the extent the US tax is allocated to foreign-source taxable income and additional conditions and limitations are satisfied. Creditable foreign income taxes include taxes borne by foreign subsidiaries on profits repatriated to a US corporate shareholder ("deemed-paid taxes").

Participation exemption – The deduction for dividends received, which serves a similar function in the case of a participation in a subsidiary (but not a branch or a PE), generally is not available for dividends received from foreign corporations (except in certain cases where the foreign corporation has ECI).

Holding company regime – No

Incentives – Incentives include numerous credits for special types of activities (including R&D), a deduction for qualifying domestic production activities and various temporary "expensing" provisions to accelerate the benefits of depreciation deductions.

Withholding tax:

Dividends – The gross amount of dividends paid by a domestic corporation to a foreign corporation generally is subject to a 30% withholding tax, unless the rate is reduced under a tax treaty or the income is ECI. Dividends paid by a narrow class of "grandfathered" 80/20 companies (a domestic corporation that derives at least 80% of its income for the three-year testing period from active foreign business (its own or its subsidiaries)) existing before 2011 are eligible for relief from gross-basis tax in the hands of foreign corporations.

Dividends received by a foreign corporation from another foreign corporation out of the latter's earnings attributable to ECI are not subject to US withholding tax; the branch profits tax (see above under "Taxable income") serves as a substitute for shareholder-level taxation of such earnings.

Interest – The gross amount of interest received by a foreign corporation from US sources generally is subject to a 30% withholding tax, unless the rate is reduced under a tax treaty or a statutory exemption applies.

Interest that is ECI and certain interest on portfolio debt obligations, short-term obligations, bank deposits, bonds issued by state or local governments and debts of grandfathered 80/20 companies generally may be exempt from withholding tax.

Royalties – Royalties received by a foreign corporation for the use of property in the US are subject to a 30% withholding tax, unless the rate is reduced under a tax treaty or the income is ECI.

Technical service fees – There is generally only a tax on fees for personal services, including technical services, if the services are performed within the US. If the services are performed in the US, such fees typically would be ECI.

Branch remittance tax – The US imposes a branch profits tax, as discussed under the "Taxable income" section of "Corporate taxation."

Other – Any other income, gain or profit characterized as "fixed or determinable, annual or periodic" (FDAP) is subject to a 30% withholding tax, unless the rate is reduced under a tax treaty or the income is ECI. A nonfinal tax also must be withheld on proceeds from the disposition of US real property interests (10%) and by partnerships on their ECI allocable to foreign corporate partners (35%).

Other taxes on corporations:

Capital duty – No

Payroll tax – The employer must withhold federal, state and local income taxes from employee wages (where applicable) and must remit these taxes to the respective government agencies. The employer also must pay federal and state unemployment taxes (where applicable) and, as noted below, social security taxes. The federal unemployment insurance rate is 6% on the first USD 7,000 of each employee's wages. State unemployment insurance, mandatory in all 50 states and the District of Columbia, varies widely. The employer receives a credit, up to a maximum of 5.4% (5.1% for states classified as "credit reduction states" that have outstanding FUTA loans), against the federal tax for amounts paid to state unemployment insurance funds.

Real property tax – Tax generally is imposed by the local governments at various rates.

Social security – Social security taxes are comprised of old age, survivors and disability insurance (OASDI), and "hospital insurance" (also known as "Medicare"). The taxes generally are borne equally by the employer and the employee, with the employer responsible for remitting each employee's portion to the federal government. The OASDI tax is imposed on the first USD 118,500 of wages, at the combined rate of 12.4%. The Medicare tax is imposed on total wages, at the combined rate of 2.9% (plus an additional 0.9% for wages above a certain threshold).

The employer's portion of social security taxes is deductible for income tax purposes. Persons who are self-employed are subject to a separate tax that is comparable to the social security tax paid by employers.

The US has totalization agreements in force with over 20 countries to eliminate dual social security taxation and to help ensure benefit protection for employees.

Stamp duty – Documentary stamp taxes maybe imposed at the state level."Stamp" taxes also may be imposed on items such as alcohol and tobacco.

Transfer tax – Transfer taxes may be imposed at the state level.

Other – The federal government imposes a variety of excise taxes, in addition to the social security taxes on wages described above. In addition, the 50 states and the District of Columbia, as well as local governments, impose various income, franchise, gross receipts, license, stamp, estate, property and other taxes based on the capital of a corporation.

Anti-avoidance rules:

Transfer pricing – The tax authorities may adjust income in related party transactions that are not at arm's length. Detailed regulations prescribe the scope, specific methodologies and principles.

Documentation is required. Advance pricing agreements, both bilateral and unilateral, may be negotiated.

Thin capitalization – The "earnings stripping" rules restrict the ability of US (and certain foreign) companies to claim an interest deduction on debt owed to, or guaranteed by, certain non-US related persons (and other related persons exempt from US tax). The rules generally apply where the debt-to-equity ratio of the payer exceeds 1.5 to one and the payer's "net interest expense" exceeds 50% of its "adjusted taxable income" for the year. Disallowed interest that is not currently deductible may be carried forward and deducted in future years if certain conditions are satisfied.

Controlled foreign companies – Certain types of income of controlled foreign corporations (CFCs) are included currently in the taxable income of "US shareholders" (US persons that own at least 10% of the foreign corporation's voting stock). A CFC is a foreign corporation, more than 50% (by vote or value) of whose stock is owned (directly, indirectly or by attribution) by "US shareholders."

Disclosure requirements – Corporations with USD 10 million or more in assets are required to file Schedule UTP, disclosing information about tax positions treated as "uncertain" for financial statement purposes.

Foreign Account Tax Compliance Act (FATCA) rules, which are designed to prevent US persons from evading US tax through foreign accounts and foreign entities, are enforced by the imposition of a 30% withholding tax on certain categories of US-source income, and on the gross proceeds of post-2019 dispositions of instruments giving rise to US-source dividends or interest, in situations where insufficient information is provided, or insufficient due diligence is performed, by foreign financial institutions (FFIs) or nonfinancial foreign entities (NFFEs) with respect to whether the ultimate owners of financial accounts or foreign entities are US persons.

These FATCA rules are in addition to other rules requiring that details of transactions, holdings and tax positions be disclosed on US tax returns, or by US payers and withholding agents, depending on the nature and size of the transaction.

Other – The US has numerous structure-specific regimes, including the anti-inversion and PFIC provisions.

Compliance for corporations:

Tax year – A corporation may adopt as its tax year a fiscal year consisting of 12 months and ending (except in the case of a 52/53- week year) on the last day of any month. Special rules apply in determining the permitted or required taxable year of certain entities (e.g. CFCs).

Consolidated returns – A group of domestic affiliated corporations may file a consolidated tax return if certain requirements are met, most particularly that the parent company must own directly 80% or more of the stock of at least one subsidiary in the group, and each subsidiary in the group must be at least 80%-owned directly by the parent and/or other group subsidiaries.

Filing requirements – For taxable years beginning after 31 December 2015, a C corporation generally must file its income tax return by the 15th day of the fourth month following the end of its taxable year (previously, the deadline was the 15th day of the third month following the end of its taxable year). Thus, the due date of the tax return (without extension) for C corporation filers with a calendar year end is 15 April rather than 15 March. However, for C corporations with a fiscal year ending 30 June, this change is delayed and will take effect for taxable years beginning after 31 December 2025.

C corporations with a calendar year end may receive an automatic five-month filing extension if an extension form is filed (previously, they received a six-month extension) for tax years beginning before 1 January 2026. A C corporation with a 30 June year end may receive an extension of seven months to file its return for tax years beginning before 1 January 2026. For taxable years beginning on or after 1 January 2016, an automatic six-month extension will apply to all C corporations, regardless of year end.

For taxable years beginning after 31 December 2015, an S corporation (a passthrough entity that is transparent for US tax purposes) must file its tax return by the 15th day of the third month following the end of its taxable year. Thus, the original due date for a calendar year S corporation is 15 March.

An S corporation is allowed a six-month extension of time to file its tax return.

The deadlines for state income tax returns and extensions may differ from the federal due dates and extensions.

Related tax must be paid on or before the due date of the income tax return.

Other filings may be necessary on a quarterly or other basis. Quarterly estimated tax payments generally are required.

Penalties – US tax rules include a comprehensive set of penalty and interest provisions for failure to pay and failure to file, with relevant amounts generally determined based on the specific form or tax code section at issue.

Rulings – Taxpayers may request a private letter ruling, to be issued relative to a specific taxpayer and specific transaction or series of events. Prefilling agreements also are available.

Personal taxation:

Basis – All US citizens and residents, including resident aliens and citizens who reside outside the US, pay federal tax on their worldwide income, with credits for foreign income taxes (subject to certain limitations). Nonresident aliens are taxed only on ECI and US-source non-ECI. Special taxing rules may apply to former US citizens and long-term residents upon or after expatriation. Most of the 50 states and the District of Columbia also collect income tax from nonresidents and individuals who reside in their territory.

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Residence – Aliens who have entered the US as permanent residents and who have not officially surrendered or lost the right to permanent US residence are taxed as US residents. Also taxed as residents are individuals who meet a "substantial presence test," which requires, subject to further considerations, either physical presence in the US for 183 days or more during a calendar year, or presence of at least 31 days during a calendar year and a cumulative presence of 183 days or more based on a weighted number of days during the calendar year (taken at whole value) and the two immediately preceding calendar years (taken at one-third value for the first preceding calendar year and at one-sixth for the second).

Filing status – The categories for individuals filing are single, married filing jointly, married filing separately, head of household or qualifying widow(er).

Taxable income – Individuals generally must include gross income from whatever source derived in their taxable income, including compensation for services (all forms of remuneration and allowances and the value of other perquisites that are not specifically exempted), dividends, interest, royalties, rents, fees and commissions, gains from dealings in property and income from a partnership. Nonresident aliens exclude non-ECI in computing taxable income; however, they are subject to US tax on the gross amounts of such income, generally collected on receipt via withholding, if the income is from US sources and not from the sale or exchange of property.

Capital gains – The excess of net long-term capital gains (generally, gains from investments held for more than one year) over net short-term capital losses (net capital gains) generally is taxed at a maximum rate of 20%. The net capital gains rate also is applicable to qualified dividends received from domestic corporations generally and from certain foreign corporations.

Deductions and allowances – Individual taxpayers are entitled to a standard deduction from adjusted gross income in calculating taxable income, or they may "itemize" deductions. Numerous credits also are available.

Tax benefits for high-income taxpayers are limited (there is a phase-out of itemized deductions and a personal exemption phase-out for single taxpayers with income above USD 259,400 (USD 311,300 for married taxpayers and USD 285,350 for heads of households (amounts indexed for inflation each year)).

Rates – Rates are progressive up to 39.6%.

In addition to the regular income tax, individuals may be subject to the alternative minimum tax (AMT), which is triggered where an individual's tentative AMT liability exceeds that individual's regular income tax liability. The AMT is imposed at a rate of 26% on the taxable excess (AMT income minus an "exemption amount") up to specified levels, and at a rate of 28% on the taxable excess above these levels. The exemption amounts for the individual AMT for 2016 are USD 83,800 for married taxpayers filing jointly and USD 53,900 for unmarried taxpayers) and will be automatically indexed for inflation thereafter.

Other taxes on individuals:

Capital duty – No

Stamp duty – The federal government does not levy a stamp tax; states may impose the levy on various instruments.

Capital acquisitions tax – No

Real property tax – Tax generally is imposed by the local governments at various rates.

Inheritance/estate tax– For US citizens and residents, a unified estate and gift tax is imposed, generally based on the net value of the transferred assets of the donor or decedent in excess of USD 5,450,000 for 2016 (USD 5,430,000 for 2015). In the case of assets inherited from a decedent, heirs generally are not subject to income tax on the appreciation of the assets in the hands of the decedent. A donee of a gift, however, is subject to tax on the appreciation of the assets in the hands of the donor.

For nonresident noncitizens, estate taxes are imposed only on property situated in the US in excess of USD 60,000. This threshold may be increased by a tax treaty.

For US citizens and residents, a gift tax is imposed on gifts made during a person's life, and it is unified with the estate tax. The gift tax is imposed on any transfer of a future interest in property and any transfer of a present interest in property that exceeds the USD 14,000 annual present interest exclusion. Certain deductions are allowed for gift tax purposes.

The top rate for estate and gift tax is 40%.

As part of its overall transfer tax system, the US imposes a generation-skipping tax (GST) on certain transfers. The states also impose various estate, gift and/or inheritance taxes.

Net wealth/net worth tax – No

Social security – See under "Corporate taxation."

Other – Individuals, estates and certain trusts must pay a 3.8% tax on net investment income over a threshold amount (individuals, USD 250,000 if married filing jointly, USD 125,000 if married filing separately and USD 200,000 in other cases; estates and certain trusts, USD 12,300). Individuals also must pay a .9% tax on wages, compensation or self-employment income that exceeds a threshold amount (USD 250,000 if married filing jointly, USD 125,000 if married filing separately and USD 200,000 if single).

Compliance for individuals:

Tax year – The tax year is the calendar year, unless a fiscal year is elected. Any fiscal year must end on the last day of a calendar month.

Filing and payment – Tax is withheld at source from employment income. Individual self-assessment tax returns are due (without extension) by the 15th day of the fourth month following the end of the tax year (or the sixth month, in the case of certain nonresident aliens). An extension of six months is granted if the taxpayer makes an election on or before the due date for the return and pays the estimated final tax due.

Penalties – US tax rules include a comprehensive set of penalty and interest provisions for failure to pay and failure to file, with relevant amounts generally determined based on the specific form or code section at issue. See also "Disclosure" under "Anti-avoidance measures."

Other – Individuals are required to file a statement with their income tax returns to report interests in specified foreign financial assets if the aggregate value of those assets exceeds certain thresholds.

Reporting thresholds vary based on whether a filer files a joint tax return or resides abroad, and are higher for married couples and taxpayers who qualify for foreign residency. For example, unmarried taxpayers living in the US have a filing requirement if the total value of specified foreign financial assets is more than USD 50,000 on the last day of the tax year, or more than USD 75,000 at any time during the tax year. Applicable assets include financial accounts, foreign stock and securities, interests in foreign entities and other financial instruments and contracts. Failure to disclose for any taxable year would subject the individual to a USD 10,000 penalty (with the continuation penalty capped at USD 50,000) and a 40% penalty on an understatement of tax attributable to nondisclosed assets.

Sales tax:

Taxable transactions – The US does not levy a federal value added tax or sales tax. Individual states and localities levy sales tax at various rates, subject to statutory requirements.

Rates – N/A

Registration – N/A

Filing and payment – N/A

Source of tax law: For federal taxes, these are the US Internal Revenue Code and tax treaties, US Treasury Regulations, federal court decisions and US Internal Revenue Service administrative guidance.

Tax treaties: Comprehensive income tax treaties are in force with over 60 countries.

Tax authorities: Internal Revenue Service

Contact Yutland:

yeahh@yutland.com

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