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Private Wealth Newsletter 2023

Fourth Edition

TAX FROM EVERY ANGLE

Editors' note

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On behalf of Baker McKenzie's Global Wealth Management Practice Group, it is our pleasure to share with our clients, friends, colleagues and readers across the globe the 2023 final edition of the Private Wealth Newsletter.

In this edition, we present the second instalment of our video interview series, showcasing our team members across offices. Juan David Velasco a Partner in our Bogota office discusses his experience with the Firm and the challenges facing clients, including privacy concerns as the wealthy come under increased scrutiny.

This edition focuses on the taxes applicable to globally mobile ultra-wealthy individuals and the tools available to governments to effectively tax cross-border wealth. Our featured article by Phyllis Townsend and Oliver Stephens considers the recent proposal by the EU Tax Observatory for a global wealth tax and the reasons this is unlikely to be implemented. Inconsistencies still exist including between jurisdictions that have signed up to existing global initiatives and even within jurisdictions. Juan David Velasco and Sofía Rodríguez consider the disparity between the rule for determining the tax base of income tax and the wealth tax on foreign investment vehicles in Colombia.

Lily Kang and Mathew Wiener highlight the potential for US tax liability to arise for non-US citizens under the lesser known substantial presence test which serves as a useful reminder for those spending time in the US.

The "Around the World" section includes an update on the decision of the Spanish Constitutional Court to uphold the solidarity tax on large fortunes, and other updates from our colleagues globally.

We wish you all the best for the holiday season and 2024.

Content

PWN meets...

In this instalment of our series of interviews, Juan David Velasco talks to us about his experience of working at the Firm and involvement with Wealth Management. Please find the link below to the full video interview.

Juan David Velasco
Partner
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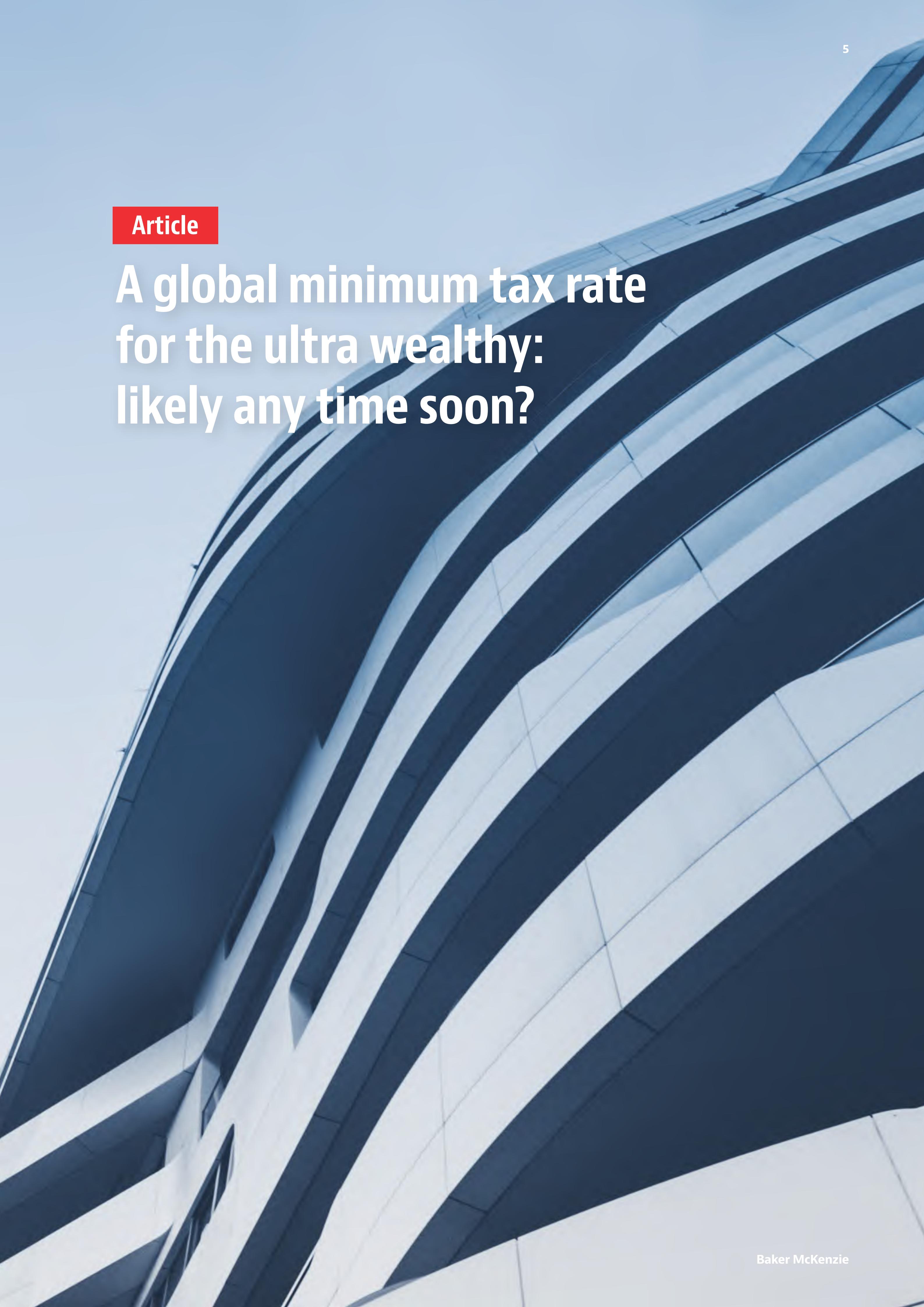

Article

A global minimum tax rate for the ultra wealthy: likely any time soon?

The EU Tax Observatory (EUTO) — the think tank credited with proposing the Pillar 2 global minimum tax regime for multinational companies that has since been endorsed by more than 140 jurisdictions — recently published another report ("Global Tax Evasion Report 2024" or "Report"). Among other recommendations, the Report proposes another global minimum tax rate, this time aimed at the global ultra wealthy, and the creation of a Global Asset Registry to facilitate this. For reasons set out in this article, we consider that both recommendations are unlikely to be implemented any time soon. Instead, measures building on the existing domestic and international tax framework and focusing on the tax and reporting obligations of big business, including strengthening Pillar 2, are more likely. However, those who could be impacted by these recommendations if implemented would be well advised to watch this space.

Six findings and six recommendations

The Report (the Global Tax Evasion Report 2024) lists "Six main new findings on the dynamic of global tax evasion and international tax competition":

1. The automatic exchange and reporting of bank information has contributed significantly to better identification of tax evasion/avoidance.
2. Despite current international anti-avoidance initiatives and measures from the Base Erosion and Profit Shifting (BEPS) process, there remains persistent profit-shifting to tax havens by high-net-worth individuals (HNWIs).
3. Pillar 2 has been dramatically weakened and rendered "largely toothless" by a series of loopholes and carve-outs.
4. Governments are competing to attract HNWIs with beneficial tax regimes, "reducing the progressivity of tax systems" and "fueling inequality". The Belgian, UK and Dutch regimes are called out as the most popular regimes (by number of beneficiaries).
5. There are very low effective tax rates on HNWIs globally. In particular, the effective tax rates of billionaires appears significantly lower than those of all other population groups, being between 0% and 0.5% expressed as a percentage of their total wealth.
6. A global minimum tax on HNWIs would raise large sums (a minimum effective tax rate on billionaires equal to 2% of their wealth would generate nearly USD 250 billion from less than 3,000 individuals).

The Report culminates in the following six recommendations:
1. Reform the current global minimum corporate tax

(Pillar 2) proposals to implement a 25% (rather than 15%) rate and remove the loopholes and carve-outs.
2. Introduce an annual global minimum tax for the world's billionaires equal to 2% of their global wealth on a global basis — the Report states that this would only ever operate as a "top up" tax and therefore would not create double taxation, but collecting any tax "deficit" could, if necessary, extend to increasing the tax due in those countries in which the HNWI's wealth is generated (e.g. countries in which the HNWI's businesses generate sales).
3. Institute mechanisms to tax HNWIs who have been long-term residents in a country and choose to move to a low-tax country — the Report recommends that the tax should remain payable in the HNWI's original country of residence, possibly for a duration proportionate to the length of the original residency.
4. Implement unilateral measures to tax multinational companies and billionaires in case global agreement / measures are not achieved or fail.
5. Create a Global Asset Registry to capture the value of worldwide assets, wherever held, and particularly asset classes considered high-risk for tax avoidance such as art and real estate — the Report argues that this transparency would facilitate the calculation of a HNWI's global wealth, upon which the 2% minimum wealth tax would be levied, regardless of the HNWI's country of residence.
6. Strengthen the application of economic substance and anti-abuse rules.
This article is concerned with the second and fifth of these recommendations.

Global minimum tax on billionaires

With regard to the second of the EUTO's recommendations, we consider it unlikely that we will see the implementation of a global minimum tax on billionaires or other HNWIs along the lines proposed by the EUTO any time soon.

Many countries are likely to oppose the introduction of such measures. As the Report itself acknowledges, from a single-country perspective, the use of preferential tax regimes to attract high-income or high-wealth individuals can enhance tax collection and boost domestic activity, including output and employment. Particularly, emerging market countries such as India and China, which are witnessing the emergence of an increasing number of "homegrown" ultra-wealthy individuals, are unlikely to introduce such measures to the detriment of their domestic economic performance.

Even if steps are taken by countries to implement measures contributing to a global minimum tax on wealth, we may see a significant weakening of such measures through the introduction of carve-outs and loopholes, both at a national level and (if the experience of the "toothless" Pillar 2 proposals is anything to go by) at the international level. At a national level in particular, the experiences of domestic wealth taxes demonstrate the significant, competing pressures governments face in formulating tax policy and that may in many cases outweigh any countervailing pressure to ensure that the global ultra wealthy pay a minimum rate of tax on their global wealth. For example, there are pressures to preserve countries' cultural heritage, often resulting in reliefs and exemptions relating to artwork, antiques and other culturally significant assets. Similarly, pressures to support and nurture entrepreneurship and investment often result in carve-outs relating to business assets. Importantly, such carve-outs are likely to present HNWIs with planning opportunities to mitigate their overall tax exposure, with the potential to undermine the effectiveness of the global minimum wealth tax regime.

A tax calculated on the basis of an individual's global wealth is very ambitious due to difficulties in valuing wealth. Wealth takes many forms, some of which are difficult to value, particularly in the case of non- or infrequently traded assets. However, the alternative — exempting such assets from an assessment of the taxpayer's wealth — could once again create planning opportunities that could undermine the minimum tax regime. In relation to the valuation of private businesses, which are an important form of wealth among HNWIs, the Report acknowledges that there would be valuation difficulties. Its suggested solution is to "apply the valuation multiples observed for similar listed businesses in the same industry". However, a comparison to listed businesses assumes that the businesses owned by the HNWI taxpayer are of a size comparable to listed businesses, which will not always be the case. On this issue, the Report concludes that internationally-agreed harmonized valuation rules would need to be developed and formalized in a global agreement, which we would venture to say is no easy undertaking.

In terms of tax compliance and administration, we anticipate that a global minimum tax based on global wealth is likely to be very costly if the value of the taxpayer's assets must be updated on an annual basis, particularly in relation to those assets that are difficult to value and that are not required to be valued for the purpose of any other tax. Conversely, if asset values

are to be updated less frequently, this could increase distortions as compared to real-time wealth values. By comparison, the valuation of assets under an estate tax, inheritance tax or other gift tax is required only once: at the time of the transfer of assets between donors and recipients. Similarly, income flows (including realized capital gains) tend to be easier to value than capital stocks. From the perspective of efficiency and administrative cost, the Report's proposed annual minimum tax based on global wealth does not compare favorably.

Turning to the information burden on countries seeking to introduce and enforce such a minimum tax, the Report acknowledges in its proposal that "each country would need to be able to identify global billionaires and their global tax payments, to compute their tax deficit" and that they:

Would also need to establish from which countries their wealth originates (e.g., which businesses they own, the geography of the sales made by these businesses, etc.), to compute the portion of the tax deficit they would collect.

As the Report notes, this would require "significant statistical progress." This is said by the Report to motivate its call for improvements including the creation of a Global Asset Registry. However, for reasons we have set out below, we consider that this too is unlikely to materialize any time soon.

Global Asset Registry

The Report envisages "a registry combining information from all available national and international sources." Its rationale is that this would enable:
Substantial progress not only in the fight against tax evasion, but also in the fight against money laundering and the financing of terrorism, in the monitoring of financial stability, and more broadly in the regulation of inequality and globalization. In particular, it could be used as a key input to implement the global minimum tax on billionaires described above.

At present, we are a long way from the centralization of information that the Report proposes (and, indeed, requires for the implementation of its proposed global minimum tax). As the Report notes, "information on various classes of assets and their ownership exists but remains fragmented in private companies, banks, (incomplete) national beneficial ownership registries, central securities depositories, and financial authorities." Against this backdrop, the proposal for a comprehensive Global Asset Registry on the scale envisaged by the Report is again ambitious.

The Report goes further in calling for public access to such information, arguing that:

The multiplication of tax data available to tax administrations empower them to fight tax evasion. Public scrutiny can help by empowering civil society and journalists to monitor high-profile, public interest tax affairs, by building tax morale and citizens' trust in government. There is also evidence that transparency can increase tax compliance and therefore tax revenues.

What the Report does not address is that wealthy individuals often have good reasons for not wishing their information to be public. Laying bare for public inspection the full amount of the resources of some individuals could make them vulnerable, in the worst cases, to violent crimes such as kidnapping or extortion. For others, the tensions, pressures and distortions that such disclosure can introduce into relationships — whether personal, business or otherwise — is reason enough to maintain discretion around their total wealth. The Report makes no mention of these considerations, which seems to be an omission given the ruling of the European Court of Justice in November 2022, which struck down the requirement for public access to beneficial ownership registries in EU member states on the basis that "the general public's access to information on beneficial ownership constitutes a serious interference with the fundamental rights to respect for private life and to the protection of personal data" (and following which at least seven countries removed their beneficial ownership registries from public access).

Whatever the Report's reasons for calling for public access to its proposed Global Asset Registry, it is clear that such developments will not be possible without a wide-ranging and in-depth discussion on their possible implications.

What's next?

Given the challenges of introducing the first two of the Report's proposals, we envisage that changes in the tax treatment of the globally wealthy and internationally mobile are more likely to focus on building on existing tax frameworks.

At a national level, reform of estate tax and capital income tax regimes are likely to be considered more feasible from the perspectives of efficiency and administration, as the frameworks for such taxes already exist. In some cases, this could extend to the introduction or development of exit taxes in countries that do not already have these, potentially along the lines recommended in the Report's third recommendation (to institute mechanisms to tax HNWIs who have been long-term residents in a country and choose to move to a low-tax country). Arguably, exit taxes should also be accompanied by a notional uplift in the base cost of an individual's assets when they assume residency in a new jurisdiction. The adverse impact of such reforms on the attractiveness of the country to HNWIs may be more limited than the introduction of a wealth tax, and may help to improve retention of HNWIs, particularly in those countries seeing an increase in numbers of "homegrown" HNWIs.

At an international level, for the time being, it seems that governments are focused on the taxation of multinational big business, rather than individuals. In particular, it is widely acknowledged (including by the Report) that the carve-outs and loopholes of the Pillar 2 regime are significant, so we may see reform here. In the short or medium term, reforms aimed at improving the effectiveness of this regime (including to reduce these carve-outs and loopholes) seem significantly more likely than the introduction of a global minimum tax on billionaires or the creation of a Global Asset Registry. In this respect, it remains to be seen whether the Report's first recommendation (to reform the international agreement on minimum corporate taxation to implement a higher rate and remove loopholes) or even its fourth recommendation (to implement unilateral measures to collect some of the "tax deficits" of multinational businesses and wealthy individuals) may soon be echoed in legislative proposals at a national and international level.

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Article

Disparity between the rule for determining the tax base of income tax and wealth tax on foreign investment vehicles

Introduction

The wealth tax has been a constant in the history of taxation in Colombia: It has been in and out of the Colombian tax framework for the last 87 years, with the government's main objective being to tax high levels of wealth and generate easy revenue. The latest tax reform enacted on 13 December 2022 — Law 2277 of 2022 — reintroduced a permanent wealth tax as of 2023 that generates a mismatch between the tax base for the wealth tax and income tax in the tax year 2023.

The wealth tax is levied on (i) resident individuals in relation to their worldwide assets, (ii) non-resident individuals in relation to their assets held in Colombia, and (iii) certain foreign companies that have assets in Colombia other than the types of investments in relation their assets held in Colombia. The tax is applicable to net assets equal to or greater than 72.000 UVT [1] (approximately COP 3 billion for 2023).

Summary

The rule for determining the tax base of the new wealth tax introduced by Law 2277 of 2022 brought clarity to the taxpayer on the reportable asset value based on the principle of fiscal transparency, but created disparity with the rule for determining the tax base of income tax.

Income tax base

The first formal approach within the Colombian tax legal system on investments in private interest foundations, trusts, insurance policies with a material savings component, investment funds or any other fiduciary business ('foreign investment vehicles') in Colombia, came with Law 1739 of 2014, on the normalization tax for that year.

In the subsequent tax reform — Law 2155 of 2021 — this provision evolved to also regulate the tax base of income tax, on the following terms:

For all Income Tax purposes, foreign private interest foundations, foreign trusts, insurance with a material savings component, investment funds or any other foreign fiduciary business are assimilated into trust rights held in Colombia. Consequently, their equity value will be determined based on the historical tax basis or the commercial self-assessment established by the taxpayer with technical support, and for the calculation of the tax base, the principle of transparency will be applied to the underlying assets.

The principle of fiscal transparency, regulated in Article 102 of the Colombian Tax Code (CTC), provides that beneficiaries of fiduciary agreements must include in their income tax returns the income, costs and expenses generated by the trust or private interest foundation with the same tax conditions, such as source, nature, deductibility and concept, that would be included if the activities that generated them were developed directly by the beneficiary.

Although the above rule was introduced in the articles regulating the now obsolete normalization tax, in Revenue Ruling 908676 of 2021, the Colombian Tax Authority (CTA) clarified the broad application of the rule to income tax in force under Law 2155 of 2021.

1. *UVT: Taxable Value Unit equivalent to COP 42,412 for 2023*

For the CTA, the expression "for all income tax purposes" meant that the normalization tax rules would have to be complied with for the purposes of income tax returns for the years 2020 and thereafter, if the foreign investment vehicles referred to in the provision were used while the provision was in force.

Wealth tax base

In addition to partially repealing Law 2155 of 2021 on the tax base, Law 2277 of 2022 reintroduced the wealth tax.

Initially, Bill 118 proposed that investments in foreign investment vehicles should be reported at the value corresponding to the underlying net asset value. Nonetheless, no regulations defining "underlying net asset value" have been proposed.

In addition to the lack of regulations determining the reportable value of the foreign investment vehicles, the initial proposal was contrary to the rules determining the tax base for income tax purposes.

Consequently, the legislator opted to maintain the principle of transparency by establishing that to determine the tax base of the wealth tax, the participants in foreign investment vehicles, must be assimilated to fiduciary rights. Therefore, the provisions of Article 271-1 of the CTC, which expressly refers to Article 102 of the CTC, would apply.

The legislator ensured that such investment vehicles issued "participations" — without defining what a participation is — and then assimilated them to "trust rights," i.e., what is delivered in consideration for the contribution made to a trust. Accordingly, the equity value of the trust rights for the settlor corresponds to participation in equity at the end of the fiscal year. Hence, participation in this type of investment vehicle must be reported under the wealth tax as a value determined in accordance with the investment that the taxpayer has in the vehicle.

However, the regulation was clear in determining that, on this occasion, the transparency rule only has effects on the WT and cannot be applied to other taxes (e.g., Income Tax). The delimitation of the scope and partial repeal of Law 2155 of 2021 put an end to the uncertainty generated by the concept of "underlying net asset value," but introduced a difference in the asset value at which these rights are reported for income tax and WT purposes, for those assets that were subject to the normalization tax.

Since there is no special rule applicable to the reporting of participation in foreign investment vehicles for income tax purposes, taxpayers must abide by the general rule of Article 74 of the CTC, according to which intangible assets are stated at their tax basis equivalent to the acquisition price, plus any costs directly attributable to the preparation of the asset. Thus, the transparency regime would seem to be applicable exclusively for WT purposes, but not for income tax purposes.

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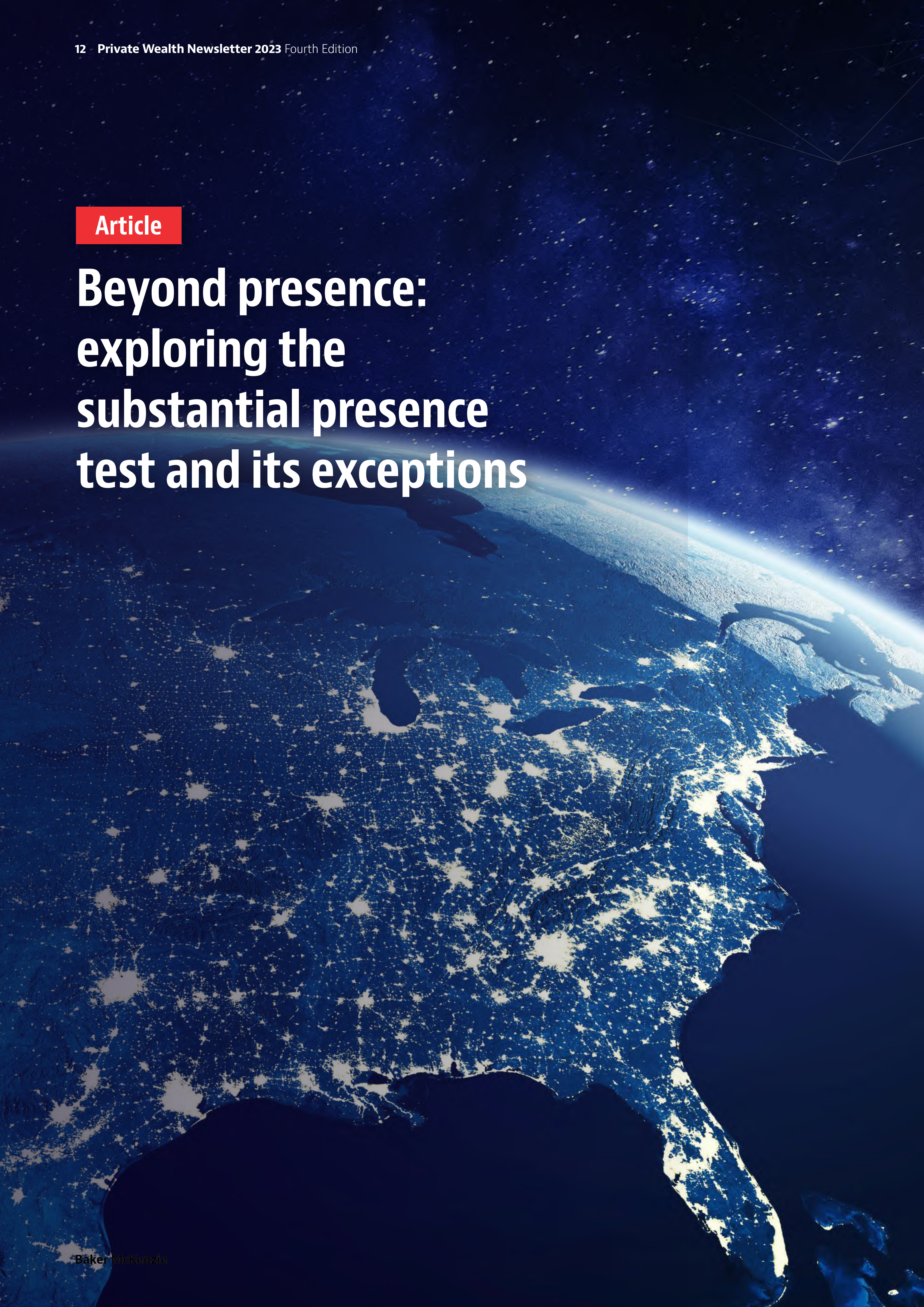
Article

Beyond presence: exploring the substantial presence test and its exceptions



Introduction

Imagine a high-net-worth couple with substantial wealth in their home country. The husband and wife are non-US citizens or green card holders. While on a short trip to the United States, the husband falls severely ill and is unable to leave the United States. Distraught and shaken, the wife stays by the bedside of her sick husband. What she least expects or thinks about while trying to focus on caregiving is an enormous US tax bill.

There could be a plethora of arguments made about why the US tax system is unfair, especially considering the circumstances. But we will do our best to stay away from the politics and instead focus on the technicality of the matter by explaining the situation from the US tax perspective. Not surprising that the reason for the enormous tax bills is the legality of the issue, or specifically the particularities of what is called the substantial presence concept under the US tax laws.

Substantial Presence Test

A person, who is not a US citizen or permanent resident, may be considered subject to US tax on his or her worldwide income, solely by being "substantially present" in the US.

General Test

An individual may be considered a US tax resident based on the results of the substantial presence test, which takes into consideration the number of days an individual is present in the US (the "Test"). [2] As a general rule, an individual that is physically present in the United States for 183 days or more in a calendar year is considered a US tax resident. [3]

An individual may also meet the Test based on the number of days of presence over a three-year period. Specifically, if an individual is physically present in the United States on at least 31 days in a given year, they will be a US resident if the sum of the following equals 183 days or more:

(1) The actual days in the United States in the given year; plus
(2) One-third of his/her days in the United States in the immediately preceding year; plus
(3) One-sixth of his/her days in the United States in the second preceding year.

Fractions of days resulting from the calculations above are allowed. Moreover, an individual must include any day on which they are "physically present in the United States at any time" during the day. Thus, if an individual is physically present for only part of a particular day, that entire day is counted.

Dual Resident/Non-Resident Status

One feature of the Test is that individuals could qualify as having "dual status" if they satisfy the Test for only part of a year, e.g., an alien's "residency starting date" may be later than January 1. The individual would file as a "nonresident alien" for the beginning of the year and "resident alien" for the remainder – or vice versa for individuals who terminate their residency mid-year.

These individuals are taxable as though their taxable year were comprised of two separate periods, one in which they are US resident and the other in which they are not. In certain circumstances, the income from both parts of the year is aggregated for these individuals to determine their taxable income.

Closer Connection Exception

An individual may seek to be classified as a nonresident if they can demonstrate a "closer connection" with a foreign country on one or more particular day(s). An individual who wishes to do so must timely file a claim with the Department of the Treasury, Internal Revenue Service ("IRS") or risk being precluded from later claiming the exception.

It can happen that an individual will not become a US resident despite meeting the Test and not claiming this exception, when the IRS independently concludes the individual is a nonresident. Here the nonresident can still claim certain exclusions from income or reductions in tax if he is deemed a resident of a foreign country under the "tie-breaker" provisions of a Bilateral Tax Treaty concluded with the United States to avoid double income taxation.

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2 *The IRS checks one's passport to verify the day count.*

3 Different tests apply to determine if an individual is present for US gift and estate tax purposes compared to income tax purposes, such that an individual may be resident for income tax purposes and non-resident for transfer tax purposes.

However, the individual would then compute his US federal income tax as a US nonresident. Alternatively, the individual could elect to be treated as a resident alien if he would satisfy the Test the year following the year of election or obtain an extension to file until a reasonable period after the satisfaction of the Test. But to request an extension, the individual must pay the US income tax for the election year as if the individual were a nonresident alien for the entire year. Though this usually will result in an overpayment, the individual can usually request a refund.

Nominal Presence Exception

The nominal presence exception allows individuals to disregard up to 10 days of presence in the United States if they stay in the US for, well, a period of ten days or less. The nominal presence exception is also called the "10 days rule." To claim the exception, an alien must be able to demonstrate a "closer connection" to a foreign country on those particular days. Note that the ten days may be accumulated over several visits to the US, e.g., two visits of five days each.

The exception for nominal presence applies only in determining an alien's residency starting date. The days spent in the US may qualify for the nominal presence exception, but they will still be included in the Test. Thus, if it is necessary to apply the lookback rule, the days will be accounted for under the Test formula. However, they might not be accounted for in determining the individual's residency starting date during the first year.

Disclosure Statement

To benefit from either the closer connection and nominal presence exceptions, the claimant must file Form 8840, Closer Connection Exception Statement for Aliens, with sufficient facts to show the individual maintained a foreign tax home and closer connection during the claimed period. The statement must be filed by the due date (including extensions) for filing Form 1040-NR, US Nonresident Alien Income Tax Return, regardless of whether the individual must file Form 1040-NR.

Medical Condition Exception

An exception to the Test also applies to "[a]liens who are unable to leave the United States because of a medical condition that arose while they were in the United States or affected by the Covid-19 emergency." Under this exception, an individual is treated as not present in the US on days when they are unable to leave due to a medical condition. It is noteworthy that this exception applies only to the ill husband in our hypothetical. It is not extended to his wife who provides her unwavering support to him.

To determine whether an individual qualifies for the exception, the IRS considers two matters: 1) whether the individual would have remained in the US anyway if the medical problems had not occurred, and 2) whether the medical condition actually arose before arrival to the US.

Intent to Leave

To properly claim the exception, the individual must intend to leave the US, but be prevented by a medical condition or problem that arises while present in the US. Whether an individual intends to leave the US on a particular day is determined based on all the facts and circumstances. However, one important factor would be the individual's original purpose for being present in the US.

For instance, if the individual's original purpose were to be in the US for a period that would be sufficient to cause the individual to be a resident under the Test, then the individual would be treated as lacking the requisite intent to leave.

If all the facts and circumstances indicate that the individual would have likely remained in the US anyway, the alien should only be permitted to claim the exception for those days after they would have left the US in the absence of the medical condition. Suppose the individual recovers and does, in fact, leave the US by the date that they originally intended. In that case, the exception is unavailable for any of the days during which the individual had a medical condition.

Once the individual can leave, a further reasonable period for making arrangements to leave the US is also not counted for purposes of the Test.

Pre- existing Condition

Individuals who come to the US for medical treatment of a preexisting medical condition are denied the benefit of this exception. A "preexisting medical condition" is a condition that existed before the alien arrived in the US, of which the alien was aware "regardless of whether the individual required treatment for the condition or problem when the individual entered the US." This suggests that the exception is available to individuals unaware of their condition before entering the US.

Consequently, the exception harshly treats individuals with manageable preexisting conditions and individuals who developed a condition during a stay in the US that later returned for treatment of that condition (though the previous stay in the US may have been excluded for the same condition).

Disclosure Statement

Individuals must generally file Form 8843, Statement for Exempt Individuals and Individuals With a Medical Condition, to claim this exception. This also must be filed by the due date for filing Form 1040-NR, regardless of whether the individual is required to file Form 1040-NR.

An individual may claim multiple medical condition exceptions on a single Form 8843 by attaching a separate statement with respect to each applicable exception. The form generally requires a signed statement from a physician supporting each claim. However, due to the Covid-19 pandemic, the IRS modified the requirements for completing Form 8843 during the calendar year 2020. Claimants may file the Form without a physician's statement to cover a single period of up to 30 consecutive days in 2020 (the "30-day medical condition exception").

In lieu of a physician's statement, individuals claiming the 30-day medical condition exception should retain documentary evidence that substantiates their condition, their inability to leave due to the condition, and the period of the condition. These documents should not be submitted with Form 8843, but the individual should be prepared to produce them if requested.

Penalty

Individuals who claim the medical condition exception, but fail to timely file Form 8843 for a given year, will be required to include all days of presence in the US for that year.

However, this penalty might not apply if the individual can show by clear and convincing evidence that they took reasonable action to become aware of the filing requirements and significant affirmative steps to comply with them. The IRS may disregard the individual's failure when it is in the best interest of the US government to do so.

Applicability to Immediate Family

The medical condition exception also harshly treats any family members who remain in the US to provide care or comfort to the individual with the medical condition. Considering the basic importance of family support to a patient's physical and mental recovery, family members end up holding the short end of the stick under the current income tax law.

Students' and Athletes' Exemption

Exemptions for Certain Students, Teachers, and Trainees on Valid Visas

An individual temporarily present in the US under certain non-immigrant visas may benefit from a limited exemption under the Test.

In general, the days an individual spends in the US are excluded for purposes of the Test if:

- The individual is admitted temporarily to the US as a non-immigrant on one of the enumerated non-immigrant visas, such as a student (F1) visa, and
- The individual substantially complies with the visa requirements.

An individual is deemed to substantially comply with visa requirements if they do not engage in activities prohibited by the US immigration laws, which could result in the loss of the visa. For example, a student with an F visa is prohibited at least from accepting unauthorized employment and maintaining a course of study that is not considered full-time. The IRS is authorized to independently inquire into the individual's compliance. But it is generally insufficient for an individual to show substantial compliance with visa requirements merely because the visa has not been revoked.

The exemption is generally unavailable for individuals who have been exempt as a teacher, student, or trainee for more than five calendar years unless the individual can establish they do not intend to reside permanently in the US. In this context, the IRS will look at all the facts and circumstances to decide on an individual's intentions.

Qualifying Teachers, Students, and Trainees

Teachers, students, and trainees might be exempted if they hold an F, J, M, or Q visa.

- F non-immigrant visas apply to individuals who wish to study as full-time students at certain eligible academic educational or language-training programs in the United States.
- J "non-immigrant" visas are for participants in certain eligible exchange programs designated by the US Department of State, designed to promote the interchange of persons, knowledge, and skills in education, arts, and science between the US and other countries.
- M non-immigrant visas apply to individuals who wish to pursue certain eligible vocational or non-academic programs.
- And Q "non-immigrant" visas are for persons who wish to participate in international cultural exchange programs designated by the US Department of Homeland Security, designed to provide practical training and employment and share the history, culture, and traditions of other countries with the United States.

Others must claim an exemption based on their particular facts and circumstances.

Professional Athletes in Charitable Sports Events

An individual may also exclude days of presence in the US if they are a professional athlete present in the US to compete in a qualifying sports event, meaning an event which: (i) is organized for the primary purposes of benefiting a §501(c)(3) tax-exempt organization; (ii) all of whose net proceeds are contributed to these organizations; and (iii) utilizes volunteers for substantially all of the work performed in carrying out such event. The days on which the athlete competes qualify for an exemption, but not the days on which the individual merely practices for the event, performs promotional activities for the event, or travels to or from the event.

An individual must claim their exempt status on Form 8843. If the individual does not file the Form, but has a good reason for not doing so, their qualifying days may nevertheless be excluded from their day count. If the individual deliberately fails to file Form 8843, the result of which is to include the otherwise qualifying days in their day count — presumably because US tax resident status would result in lower US income tax — the IRS has the discretion to exclude the days of presence from the day count.

Disclosure Requirements

A qualifying athlete, teacher, student, or trainee must file Form 8843 to exempt their days of presence in the US for purposes of the Test.

In contrast with the medical condition exception (and professional athletes exemption), a failure to file Form 8843 by qualifying teachers, students, or trainees does not result in a loss of the exemption.

But like the medical condition exception, the exemption for professional athletes is not available to members of the individual's immediate family (spouse or dependent children). The exemption for qualifying teachers, students, and trainees is open to the immediate family of those individuals if their visa status derives from and is dependent on the exempt individual's visa classification.

The due date for an individual to claim any exception or exemption under the Test is the due date for their Form 1040-NR (including applicable extensions). If an individual does not have a filing requirement, their Form(s) should be filed by the due date for Form 1040-NR to the address specified on Form 8840 or Form 8843, albeit without Form 1040-NR.

Conclusion

What an unfathomable experience it must have been when the couple in our hypothetical finds the wife to be subjected to US tax on her worldwide income. The substantial presence test, working like a quiet yet unyielding "switch," has turned on the wife's non-US resident status for US tax purposes regardless of the difficult situation she was in. It is fair to say that unless properly advised, a non-US person is often completely unaware of the consequences of the substantial presence test. However, knowing and understanding the law may put you just one step ahead. All it takes for those contemplating spending time in the US is to get advice, which may potentially save them millions of dollars or at least make them aware of the potential risks.

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Around the world

France - Expiration of tax deferral in case of cancellation of shares received in consideration for a contribution under the regime of Article 150-0 B ter of the French Tax Code (Ministerial Response Woerth, JOAN 29 August 2023, Q. No 7128)

A ministerial response clarified that a capital reduction through the cancellation of the securities received in consideration for a contribution triggers the expiration of the tax deferral, as opposed to a capital reduction through a decrease of the nominal value of the shares.

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France - Clarification of the tax treatment of trust income under the French-US double tax treaty (French Administrative Supreme Court, opinion dated April 18, 2023, n°406825)

The French Administrative Supreme Court asserts that non-discretionary revocable trusts established in the United States whose beneficiaries are U.S. citizens who are French tax residents, are not considered as transparent under French tax law and, therefore, under the double tax treaty between France and the U.S.

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France - Obligation for French tax residents to declare foreign bank accounts: clarification for corporate officers of commercial companies holding bank accounts outside of France (Ministerial Response Mizzon, No 06868 : JO Sénat August 31, 2023, p. 5186)

In a ministerial response dated August 31, 2023, the French Minister of the Economy recently commented on the obligation for French tax residents to annually declare their foreign bank accounts, clarifying that the fact that a person holds a shareholding in a foreign company or is its corporate officer is not in itself sufficient to fall within the scope of this reporting obligation.

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Spain - The Spanish Constitutional Court upholds the temporary Solidarity Tax on Large Fortunes

The Plenary of the Constitutional Court has dismissed the appeal of unconstitutionality filed by the Council of the Community of Madrid against the Temporary Solidarity Tax on Large Fortunes (TLF) established by Act 38/2022, of December 27 (Article 3). The ruling, backed by the progressive majority of judges, holds that the TLF does not imply an invasion of the state into the tax jurisdictions of the autonomous communities.

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South Africa - Developments in the VAT and residential property realm - A move towards a clearer picture? (Part 1)

This article, in two parts, discusses the VAT implications in South Africa where developers let residential property on a temporary basis, and highlights some of the discrepancies in the application of the relevant provisions of the Value Added Tax Act and how the draft Taxation Laws Amendment Bill, 2023 seeks to address these.

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Saudi Arabia - New KSA Income Tax Law and Procedural Law published for Public Consultation

On 25 October 2023 the Zakat, Tax and Customs Authority ("ZATCA") published a new corporate income tax (CIT) law for public consultation. The new CIT law is a complete overhaul of the current CIT law, which has remained mostly unchanged since its enactment in 2004.

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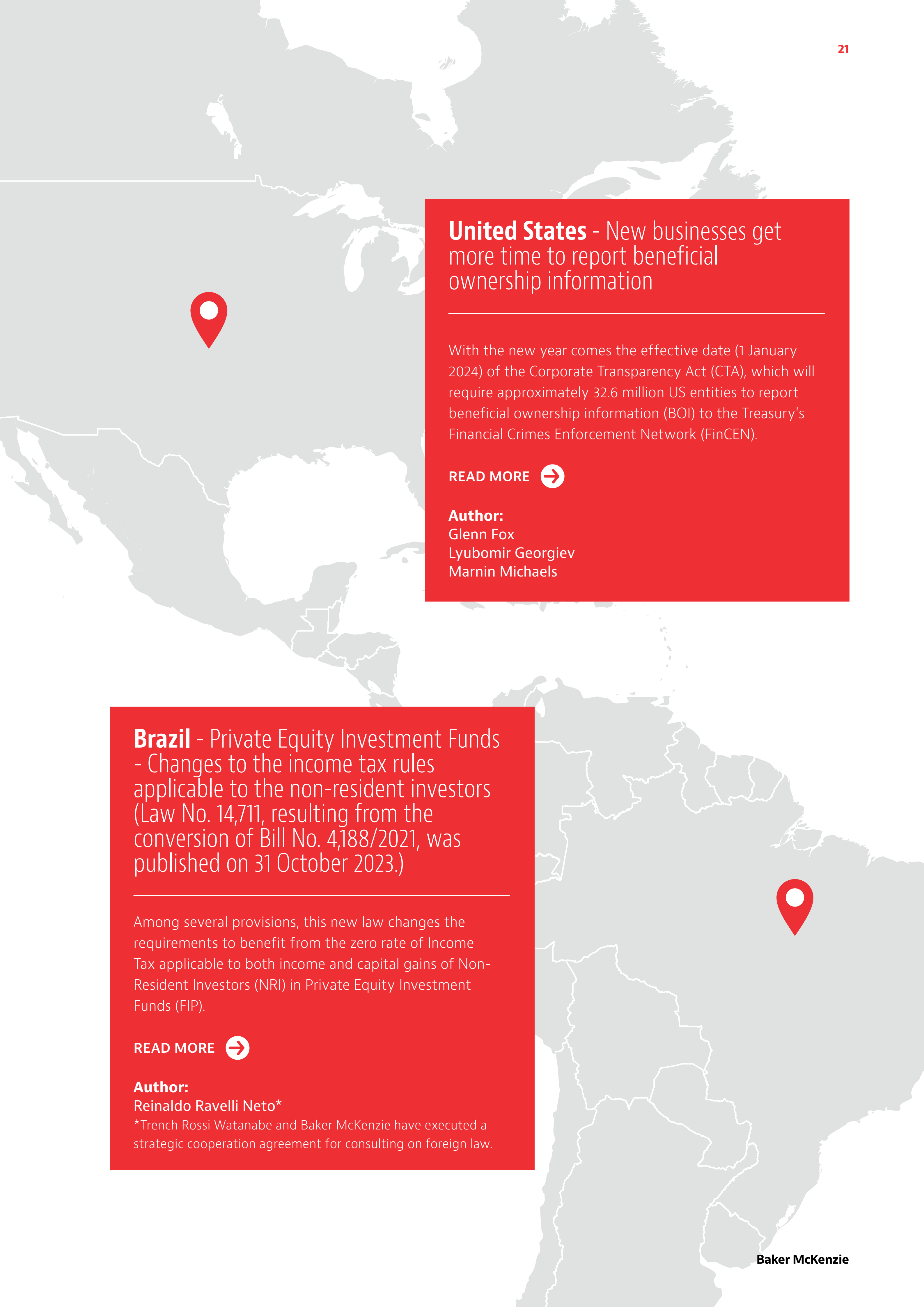

United States - New businesses get more time to report beneficial ownership information

With the new year comes the effective date (1 January 2024) of the Corporate Transparency Act (CTA), which will require approximately 32.6 million US entities to report beneficial ownership information (BOI) to the Treasury's Financial Crimes Enforcement Network (FinCEN).

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Brazil - Private Equity Investment Funds - Changes to the income tax rules applicable to the non-resident investors (Law No. 14,711, resulting from the conversion of Bill No. 4,188/2021, was published on 31 October 2023.)

Among several provisions, this new law changes the requirements to benefit from the zero rate of Income Tax applicable to both income and capital gains of Non-Resident Investors (NRI) in Private Equity Investment Funds (FIP).

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United States - Yes courts can do that

Two recent tax controversies demonstrate the authority of US courts in situations where a taxpayer's assets are held in a country different than the taxpayer's country of residence. In United States v. Kelly, a US person held assets in a Swiss bank account and failed to file a Foreign Bank Account Report (FBAR), and the court ordered repatriation of those assets to the United States.

In Puri v. United States, an Indian taxpayer held assets in a US bank account, and the United States Supreme Court denied certiorari, finalizing the district court's order that denied taxpayer's motion to quash an administrative third-party summons issued by the IRS.

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Argentina - Tax on the highest income from employment relationships, retirements and privilege pensions

On 6 October 2023, Law 27,725 was published in the official gazette, promoted by the government, through which the fourth category of income tax was eliminated as of the 2024 fiscal period. It will be replaced by a new tax called "tax on the highest income from employment relationship, retirements and privilege pensions" (hereinafter referred to as the "Tax on the Highest Income").

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Argentina - Low or null taxation jurisdictions (LNTJs) and a favorable Court precedent

The Federal Tax Authority (FTA) published a list of low or null-taxation jurisdictions. According to the Argentine Income Tax law, LNTJs apply an income tax rate of below 15%. You can access the Spanish list here.

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Argentina - Beware of the ownership of real estate and the "center of vital interests" test for tax residency purpose

Expatriates, "citizens of the world" and their families have to deal with tax residency, double residency and their tax implications when they travel and move around the world for labor, tax planning and/or family reasons.

In a recent decision of the Argentine Fiscal Tax Court (FTC) re: The Taxpayer, dated 24 August 2023, the FTC concluded that the Taxpayer was an Argentine tax resident because he owned various properties located in Argentina and his "center of vital interests" was also in Argentina.

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Argentina - Increase in the collection regime from 45% to 100% on all operations reached by the tax on the acquisition of foreign currency

On 23 November 2023, Resolution No. 5450/2023 ("Resolution") was published in the official gazette. With respect to all transactions covered by the Tax on the Acquisition of Foreign Currency ("Tax"), the Federal Tax Authority (FTA) increased the collection regime on the acquisition of foreign currency from 45% to 100%. The Resolution will be applicable to operations carried out as of 23 November 2023.

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Malaysia - Proposed mandatory beneficial ownership reporting requirements under the New Companies (Amendment) Bill 2023

On 10 October 2023, a new Companies (Amendment) Bill 2023 ("2023 CA Bill") was tabled for its first reading at the Malaysian Parliament. The 2023 CA Bill purports to further augment corporate transparency and accountability, and as such, introduces, among other things, new legal requirements in the CA 2016 for Malaysian companies to collate and report beneficial ownership information to the Companies Comission of Malaysia.

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Singapore - New tax on gains from the disposal of foreign assets

A new Section 10L in the Income Tax Act 1947 (ITA), which taxes gains received in Singapore from the sale of foreign assets by businesses without economic substance in Singapore in the Income Tax (Amendment) Bill 2023, has been passed by Parliament on 3 October 2023 and will come into force on 1 January 2024. This enactment aligns Singapore's tax regime with international norms.

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Thailand - Offshore income received before 1 January 2024 can be brought into Thailand in 2024 or later without being subject to Thai personal income tax

According to the Revenue Departmental Order No. Por. 162/2566 re: Income Taxation under section 41, paragraph two, of the Revenue Code, dated 20 November 2023 ("Order No. 162"), offshore income received by Thai tax resident individuals before 2024 can be brought into Thailand in any subsequent year without being subject to Thai personal income tax. Order No. 162 is the supplemental amendment to the Revenue Departmental Order No. Por. 161/2566 ("Order No. 161"), providing additional guidance on the same matter

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