

U.S. TAXES FOR AMERICAN EXPATS

1040Abroad

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Thank you for downloading our free e-book “US taxes for Americans abroad”!

We hope you will have a better understanding of the international taxation of US after you finish reading it. We tried to cover the most important topics in an easy-to-remember way.

Let us introduce the short story behind 1040 Abroad before you proceed into the world of US taxes for expats.

Our tax firm **1040 Abroad** was founded in 2012 by **Olivier Wagne**r, who moved to the US from France where he was born and raised.

A few years later after he got his MBA, worked on Wall Street and later obtained his US citizenship.

He then moved to Canada to work in large accounting company, but soon enough he started to travel all over the world.

It was Olivier’s real-life experience: he learnt the intricacies of the US immigration process, combined with his desire to not be tied to any single country which lead him to specialize in taxes for US expats living and working abroad.

Testimonial



Renee

"I have been trying to find a good tax guy for years. This one finally made my tax situation right and even got me a refund! I definitely recommend them."

★★★★★

AUTHOR'S LETTER

Olivier Wagner, Founder of tax firm 1040Abroad.
CPA & EA specializing in International US taxation



Are you a citizen of the United States who lives abroad? Or American who moved abroad, but hasn't given up his original citizenship. Maybe you were born in the US, but have no real ties to it. Such "Accidental Americans" are more common than you might think, and many of them don't even realise they are obligated to pay US taxes.

You could be a self-employed "digital nomad" who works from several different countries in the course of the year. Despite your unconventional way of making a living, you might still owe taxes to the US because you are taxed on worldwide income.

Maybe you've recently moved from the United States, and aren't sure how this affects your filing requirements. Have you established residency in another country? Do you still derive income from the US or in another country?

You may have been told that you don't owe any U.S. taxes on money made overseas. This is true up to a certain amount if you know how to take advantage of the proper avenues. Exclusions can cover the first $112,000 of wages (2022 number).
Most of U.S. expats do not owe any tax and they can exclude this amount. But in order to claim this exclusion, you have to regularly file your tax return and let IRS know that you are tax compliant.

There is no one one-size-fit-all answer for every American living abroad, no matter what their specific tax circumstances are. And if you don't understand the full spectrum of U.S. tax possibilities which lay before you, you could end up paying a lot more than necessary. Or worse, you could be considered tax noncompliant by the U.S. government. You may be able to evade any negative repercussions for a while, but sooner or later you will have to face up to what you've been running from.

ALL THESE FACTORS WILL CHANGE THE TAX GAME FOR YOU

You probably already know that the US is one of only two countries in the world that taxes based on citizenship. So as long as you are a US Citizen, you still have to mail in a return every year. This can be especially problematic for those who have not filed US taxes in a long time – or ever. How do you go about making sure Uncle Sam gets his due without suffering enormous penalties as you struggle to get compliant?

Our work at 1040 Abroad (and our goal in writing this book) has not been to scare you into taking action you have been avoiding. On the contrary, I and my team of U.S. expat tax experts wish to **empower the people we work with to live fuller lives and feel more confident in their actions** by taking control of their unique tax situations.

Yours in Freedom,
Olivier Wagner

PART I: INTRODUCTION TO TAXES ABROAD

CHAPTER 1 : WHAT HAPPENS IF I DON'T FILE?

The first thing to understand is that anything you owe the U.S. that you don't pay while living overseas is subject to **5% interest**. Though imprisonment is unlikely, you could face fines. Nonpayment of taxes can not only hurt your finances but your travel plans as well.

How do expatriates become compliant with the US tax system?

The 1040 isn't the only form you need to file. Many activities that seem benign would trigger specific filing requirements, and you may have to file additional forms. The rules are the same for Americans living in the US, but Americans living abroad are much more likely to have these "foreign" activities.

Failure to file these can bring hefty fines **– up to $10,000 –** if they're not turned in on time.

These forms are:

- **Form 5471** You must file this form if you own more than 10% of the controlled foreign corporation. If over 50% of the corporation is owned or controlled by US citizen it is a controlled foreign corporation.
- **Form 3520** You must file this form if you are the grantor or "substantial owner" of a foreign trust. The IRS Form 3520-A is the annual information return of foreign trust with a U.S. owner. This tax form is usually one of the attachments required when filing Form 3520. It only applies if a foreign trust has at least one U.S. owner of any portion of the foreign asset
- **Form 8621** This is for people who own stock in a Passive Foreign Investment Company (PFIC). In any cases, foreign mutual funds would also be classified as PFIC.



MOST PEOPLE OWE A LOT LESS THAN THEY THINK THEY DO, AND GETTING COMPLIANT CAN BE A MUCH EASIER PROCESS THEN YOU IMAGINED

The good news is that you've got a little more time to file. Tax returns for Americans overseas are automatically given until **June 15** to file, without having to request a special extension.

You might have a lot more to lose by not filing than by getting caught up with your taxes. You may not have to face the consequences of it today or tomorrow, but the longer you go without paying your legal dues, the more likely it is that it will eventually come back to bite you. In the next chapter, I'll tell you exactly how to go from noncompliance to being compliant in the easiest (and cheapest) possible ways.



YOU MIGHT HAVE A LOT MORE TO LOSE BY NOT FILING THAN BY GETTING CAUGHT UP WITH YOUR TAXES.

CHAPTER 2: STAYING OR BECOMING COMPLIANT

So you've decided to file your US taxes... congratulations and welcome to the club of tax-compliant US expats abroad!

Read on to find out exactly how to make it happen. As you know, **if you have lived outside of the country most of the year, you can have up to $112,000 of your income excluded** (for 2022 tax return) from federal taxes under the Foreign Earned Income Exclusion (FEIE) (Form 2555). You can also claim a credit for taxes you paid to foreign governments, the Foreign Tax Credit (FTC) on Form 1116.

Generally speaking, **if your foreign tax rate is greater than your US tax rate, we recommend claiming the FTC** as it would be more advantageous as the FEIE comes with other limitations. But don't worry, our U.S. expat tax experts will be there to help you determine the most advantageous way to file your taxes.

It is important to establish your US residence in a state which does not impose a state income tax. Many states have tax laws that mirror the federal exclusions, allowing either the FEIE or FTC for state tax purposes. California has a classification called the "Safe Harbour" rule to allow for residents of CA to be classified as non-residents for tax purposes if they leave the country on employment-related contracts. This rule can be applied if the taxpayer is outside the state of CA for at least 546 consecutive days (a year and a half) and has less than $200,000 of investment income during the year. The taxpayer can return to California for visits of less than 45 days during the year.

If you're looking to change the state of your residence for tax purposes, **keep in mind that some states do not collect income tax**. To prove that you've established a new residence, however, you would need to re-register to vote, get a driver's license in the new state and update your mailing address with your banks and others. Getting a driver's license in the new state typically requires a visit to that state. There are a few mailbox services that not only provide you a mailing address in the new state, but also guide you in the process.



MOST PEOPLE OWE A LOT LESS THAN THEY THINK THEY DO (MOST DON'T OWE ANYTHING AT ALL!), AND GETTING COMPLIANT CAN BE MUCH EASIER THAN YOU THINK

CHAPTER 3: THE ADDITIONAL CHILD TAX CREDIT

Expats with children take a note - **the Additional Child Tax Credit is generally not compatible with the Foreign Earned Income Exclusion**. To get the tax credits for children, one needs to have $3,000 of earned income for the year, and any income excluded by the FEIE does not count.

The Additional Child Tax Credit is a nice thing to have since it can mean that you get a credit of up to $2,000 per child per year and $1,400 of the amount is refundable. If you don't have any tax owing to the US, the $1,400 will be deposited directly to your US bank account.



April 15th is widely known as the due date for taxes (April 15th in 2022). If you are an American living overseas, you have an **automatic extension to file until June 15, 2022**. You do not need to file any forms to receive this extension; it is automatically afforded to any U.S. citizen living overseas.

If you need more time, you can apply for an additional extension that will give you until October 15th, 2022 to file. No response from the IRS is needed. As long as you've sent off Form 4868 by the June or April due date, your late tax return is covered. Please, **note that the extensions are an extension to file, not an extension to pay**. Interest on taxes owed start accruing on April 15. If you suspect that you will owe tax, you can attach a payment to form 4868.

GET A REFUND OF UP TO $2,000 PER CHILD PER YEAR

CHAPTER 4: UNDERSTANDING THE FORMS AND PAPERWORK



Paperwork... the bane of taxpayers everywhere. It's bad enough for Americans who live and earn their income within the borders of the US. As an American Abroad, you're going to have your own paperwork specific to your situation and your goals.

Remember – **as an overseas resident, you get an automatic extension to June 15th, and can file for extensions up until October 15th**. The deadline to file an FBAR (report of non-US bank accounts) on form FinCEN 114 is October 15th, 2022.

Filers who fail to file their 2021 FBAR by April 15, 2022, have an **automatic extension up to October 15, 2022**. The IRS can claim half your bank account for failure to file an FBAR, so it's crucial to get these forms in.

The majority of overseas residents will have to file an FBAR. But certain other forms can apply to your situation as well. Generally, the IRS will pay more attention to bigger accounts – and, will be much more comfortable imposing big fines for noncompliance on these forms.

Form 3520 is the Annual Return to Report Transactions with Foreign Trusts and Receipt of Certain Foreign Gifts. You must file this form if you are the grantor or "substantial owner" of a foreign trust. If you received over $100,000 from a foreign individual's estate or over $16,076 from a foreign corporation, you would also have to file this form.

Any payouts a student has received have to be reported on Form 3520. Pension's plans similar to a 401(k) ("defined contribution plan") are treated the same way.

Form 5471 applies if you owe more than 10% of the controlled foreign corporation. If over 50% of the corporation is owned or controlled by US citizens, it is a controlled foreign corporation. If at any point of the year you held 10% of CFC, you have to file. CFC is a corporation with more than 50% of share ownership by U.S. persons.

IF OVER 50% OF THE CORPORATION IS OWNED OR CONTROLLED BY US CITIZENS, IT IS A CONTROLLED FOREIGN CORPORATION.

CHAPTER 5: SOCIAL SECURITY

The U.S. has signed **tax treaties** with more than 67 countries, including most (but not all) of the popular destinations for expatriates.

Tax treaties are essential for multinationals doing business in a jurisdiction where they may be exposed to double taxation of income. Under these treaties, U.S. expats are taxed at a reduced rate. Sometimes, they are exempt from US taxes on certain items of income from U.S. sources.

If your host country **doesn't have a tax treaty** with the U.S. or does not cover a particular type of income, you are required to pay taxes like other U.S. citizens. If you are self-employed and reside in a country that didn't sign a totalization agreement with the US, you will be subject to the **self-employment tax of 15.3%** despite using FTC and/or FEIE.

By incorporating a foreign corporation and receiving their income in the form of wages, you are not subject to Social Security and Medicare withholding.

Note: *Tax treaties have what is known as a saving clause, which reserves the right of the United States to impose a tax on expatriates as if a treaty were not in effect.*

WARNING: **Failing to contribute to social security will impact your benefits at retirement.** You need to decide what's more important to you before making such an impactful decision.

You should understand by now that being an American citizen will always carry certain responsibilities and tax obligations, no matter where you live or work. These far-reaching policies are unlikely to change any time soon, which has left many to wonder the best way to legally get out of the system entirely.

The only way to completely eliminate your tax obligations as an American is to officially renounce your US citizenship. In the final section of this book, I'll walk you through the steps that people are taking in record number to cease being an American and break up the IRS forever.



CHAPTER 6: SOCIAL SECURITY WITHOUT A TOTALIZATION AGREEMENT

If you're living outside the US, how much can you be expected to pay into US Social Security? The answer, of course, depends on a few different factors – most importantly the existence of **totalization agreements** with your new country of residence. What? You don't know what a Social Security totalization agreement is?

The United States Government has signed totalization agreements with several foreign governments – mostly in Europe – to where US citizens living in those countries would only be responsible for paying into the other country, and not the US. Italy was the first to reach Social Security agreements with the US in 1978.

Most of Europe* followed the suit, along with Canada, South Korea, Chile, Australia, and Japan. So if you're paying into the social security systems in any of these countries, you don't have to pay into the US system.

1

How can the social security burden be addressed for expats living in countries not listed such as Indonesia?

If you live in a country with no totalization agreement, you must pay the self-employment tax on your self-employment income even if it is excludable as foreign earned income. US Expats can avoid paying the self-employment tax by creating a corporation and excluding their wages using the FEIE. Be advised – if you go this route, you'll have to file **Form 5471**, which will increae your compliance costs

2

Will not paying into the system hurt you in the long run, should you choose to return to the US for retirement?

It will if you don't have a retirement account. Generally, these outperform the social security system anyway, so with wise investing,
you should be able to build a custom retirement that saves you on taxes in the long run.

3

Is form 8965 still required?

Beginning in Tax Year 2019, Form 8965, Health Coverage Exemptions, will no longer be used. You need not make a shared responsibility payment or file Form 8965, Health Coverage Exemptions, with your tax return if you don't have a minimum essential coverage for part or all of the year.

***As of 2022, the EU countries with Social Security agreements with the US are Italy, Germany, Switzerland, Belgium, Norway, the United Kingdom, Sweden, Spain, France, Portugal, the Netherlands, Austria, Finland, Ireland, Luxembourg, Greece, Australia, Denmark, the Czech Republic, Poland, and the Slovak Republic, Hungary.**

Client Testimonial



Pete Necks

★★★★★

1040 Abroad is an expats gem

I am so pleased to have learned of 1040 Abroad. Oliver and Michelle replaced my expat tax stress with comfort and ease. They went above and beyond just completing my taxes. They followed up and corrected a CRA error, and amended my IRS return saving me a fortune. They are the very best.

Federal Tax Return

PART II: OWNING A FOREIGN CORPORATION

CHAPTER 7 : WHAT IS A CONTROLLED FOREIGN CORPORATION (CFC) AND SUBPART F INCOME?

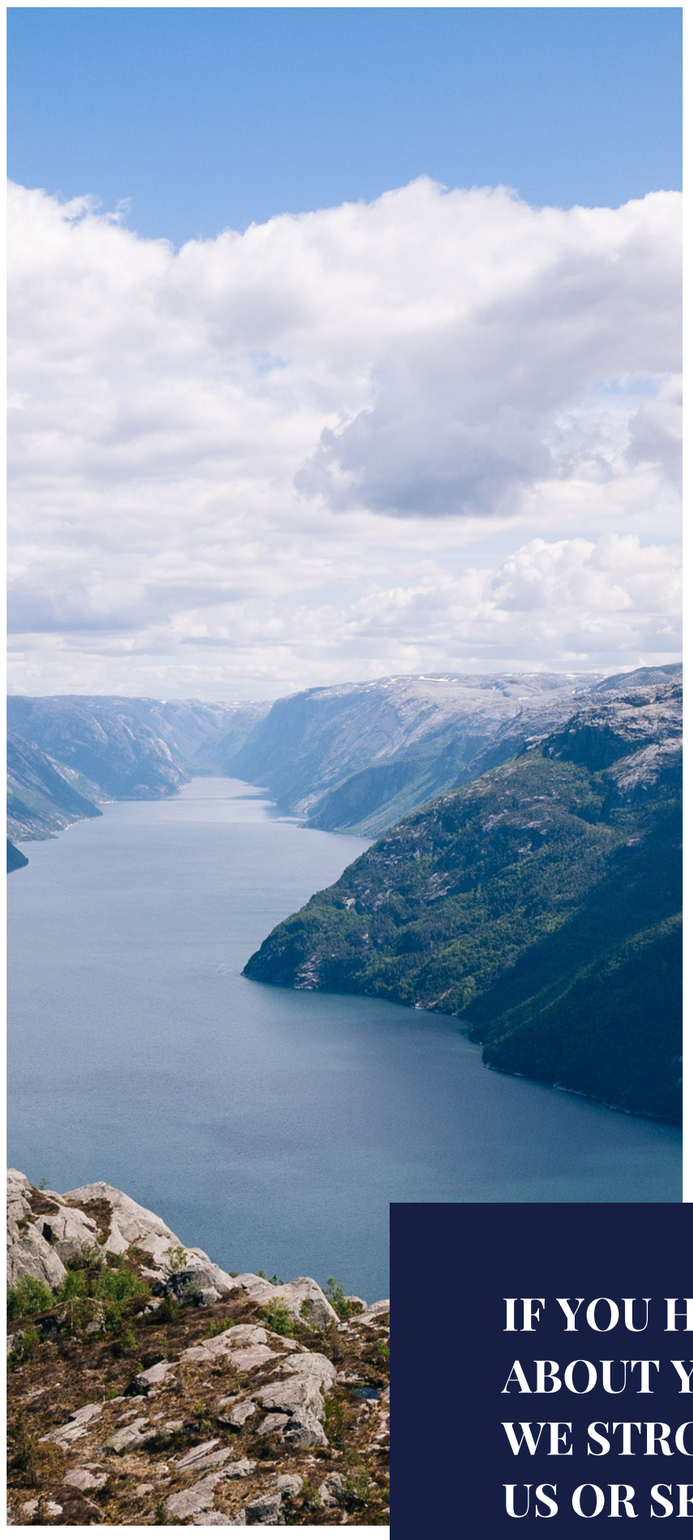
A Controlled Foreign Corporation is a foreign corporation in which more than 50% of the shares are held by U.S. Shareholders. A U.S. shareholder is a U.S. person who owns at least 10% of the shares. What does “foreign” mean in the context of business incorporation? The IRS considers only non-U.S. companies and companies which are taxed as corporations (including LLCs that elect to be taxed as a corporation) for the purpose of CFC status.

What is Subpart F?

Enacted in 1962, Subpart F tightly regulates income earned by Controlled Foreign Corporations. Generally, U.S. tax on the income of a foreign corporation was deferred until the income was distributed as a dividend or otherwise repatriated by the foreign corporation to its U.S. shareholders.

The Subpart F provisions eliminate deferral of U.S. tax on some categories of foreign income.
There is another category of income called **Global Intangible Low-Taxed Income**, or **GILTI**, that requires the recognition of a percentage of previously deferred foreign earnings. It means that almost everything is now taxed as Subpart F income or GILTI income, especially digital income.





If you own a Controlled Foreign Corporation, then you must file an annual report on **IRS Form 5471 – Information Return of U.S. Persons With Respect to Certain Foreign Corporations**. You will need to submit information regarding U.S. citizens who are shareholders, director, and officers; a listing of all U.S. shareholders and their stocks; CFC’s classes of stock and shares outstanding; a balance sheet and income statement for the tax year.

The Foreign Tax Credit applies to any taxes the CFC may have paid to its host country – the taxpayer can claim his/her share of FTC as if he/she had paid it himself/herself.

IF YOU HAVE ANY DOUBTS OR QUERIES ABOUT YOUR US TAX FILING OBLIGATIONS, WE STRONGLY ADVISE YOU TO CONTACT US OR SEEK PROFESSIONAL ADVICE.

PART III: IS THERE RELIEF FROM INCOME TAX?

CHAPTER 8: THE FOREIGN EARNED INCOME EXCLUSION (FEIE)



Many of us have tax situations that aren't so complicated. **For simple returns consisting mostly of earned income, the Foreign Earned Income Exclusion (FEIE) may be the right way to go.** It's especially useful for digital nomads and anyone who doesn't pay foreign taxes (or at a rate much lower than their US tax rate).

Under the FEIE, a certain amount of your income (up to $112,000 for the 2022 tax return) becomes excluded from income tax. To qualify for this, you have to meet a certain number of requirements that many expatriates can easily adhere to.

You have to either:

- Spend at least 330 days out of any 12-month period in a foreign country – **physical presence test**;
- Be a bona fide resident of another country – essentially meaning that you plan to stay indefinitely (the minimum requirements include being liable for taxes in that foreign country and not having claimed to be a non-resident to the authorities of that country) – **bona fide residence test.**

It's important to understand that this exclusion only applies to **foreign and earned income**. Earned income includes wages, salaries, professional charges, or other amounts paid to you for personal services rendered.

You cannot exclude income you earned while working in the US or passive category income such as distribution of earnings or profits, dividends, interest, rental income and/or IRA distributions. You must either be an employee and get a salary/wage or be self-employed and earn money in the new country.

NOTE: YOU DO NOT AUTOMATICALLY BECOME A BONA FIDE RESIDENT BY LIVING IN A FOREIGN COUNTRY FOR ONE YEAR.

IN ADDITION, ONE NEEDS TO HAVE A "TAX HOME" IN A FOREIGN COUNTRY. PRACTICALLY SPEAKING, THIS WOULD ALREADY BE MET FOR SOMEBODY MEETING EITHER OF THE TESTS ABOVE.

CHAPTER 9: FOREIGN TAX CREDIT (FTC)



A U.S. citizen or resident alien who pays income taxes in another country can claim a foreign tax credit against their U.S. federal income tax bill. You can offset your US tax liability by claiming the foreign taxes paid to another country. This way, you can bring your tax owing down to zero.

The **Foreign Earned Income Exclusion** (FEIE) **or the Foreign Tax Credit** (FTC) - which one will you use to legally reduce your taxes?

Let's look at the pros and cons of each so that you can make the most informed decision:

- The FEIE disqualifies you from claiming the Additional Child Tax Credit.
- Also, the FEIE, as the name implies, can only exclude earned income.
- The FTC can apply to all kinds of income (including passive income, although it has its own category).
- Thus, if you have a substantial amount of another kind of income, the FTC could be more advantageous.
- Using the Foreign Tax Credit, one must have paid foreign taxes, and to be able to completely offset the US tax liability such foreign tax must have been at least as much as the US tax owing. The excess (of foreign tax paid over US tax owing) can be carried forward for up to 10 years.

Hence, while the FEIE can reduce your tax liability to zero, the FTC can provide credit for future years (although this credit is not refundable).

THE FTC CAN APPLY TO ALL KINDS OF INCOME (INCLUDING PASSIVE INCOME, ALTHOUGH IT HAS ITS OWN CATEGORY).

PART IV: RENOUNCING YOUR US CITIZENSHIP

CHAPTER 10: WHY AND HOW TO RENOUNCE?

As one of only two countries with citizenship-based taxation, **all US citizens have to file a tax return regardless of where they reside** (once their income exceeds the filing threshold). People who don't plan on returning to the US may be wondering **– why am I still a citizen?** Others may not even consider themselves to be US Citizens – as they were born in the US, but built their own life abroad from a very young age. Such **Accidental Americans** are still expected by the IRS to comply with their filing requirement.

Situations like these may lead you to ask - **is there a way to end my citizenship and permanently free myself from the IRS?** The US has made it costlier in recent years, but it can be done. However, renouncing your citizenship is not a decision which should be taken lightly. In addition to the time and money involved in the process, it's something which will forever affect how easily you can return to the United States.

Additionally, **if you don't already have another citizenship in place before you renounce, you will end up stateless** and, depending on your immigration status elsewhere, might suddenly find yourself struggling to prove your identity or move freely across international borders.

Relinquishment of citizenship can be done in a number of ways. If you have taken a job with a foreign government or military or become a citizen of another country, you effectively end your citizenship with the United States. The trouble is, **the burden remains on you to prove this to the US**. If you took up foreign citizenship years ago, you will still be asked to account for all the intervening years when you become compliant with US taxes.



The government fee to renounce U.S. citizenship is $2,350. Additional costs might apply if you have to become tax compliant. You must be tax compliant for five years in order to renounce your US citizenship.

We offer Renunciation Packages specifically tailored to U.S. citizens who wish to give up their citizenship. We offer flat fees regardless of the number of forms required.

Our **Renunciation Package** is **$2,600**.

THE ONLY WAY TO COMPLETELY ELIMINATE YOUR TAX OBLIGATIONS AS AN AMERICAN IS TO OFFICIALLY RENOUNCE YOUR US CITIZENSHIP.



Your Trusted U.S. Expat Tax Services

1040Abroad

About us.

We help US Expats file their U.S. tax returns, catch up with late taxes using IRS amnesty programs and design financial strategies to maximize their wealth while minimizing their tax burden.

Why Choose Us?

Just knowing that a professional is handling your taxes reduces stress. We offer transparent flat fees so you won't have any surprises on the final bill.

Check out what our clients say about us -**TrustPilot**

Our Process

Contact us

Our team will contact you within 1 business day to explain the process. During the free consultation call our U.S. tax expert will answer your questions and give you the best solution.

Upload your information

Upload the completed Questionnaires to our secure portal together with any suporting documents you might have.

Review and file

Your return will be ready within 2 weeks, so all you have left is just sit back and relax while we take care of your taxes.

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www.1040abroad.com

Client Testimonial



Chris

★★★★★

Knowledgeable, friendly staff. Quick to answer all questions, they will put your mind at ease when dealing with complicated tax issues that all US citizens living abroad may face. Highly recommended.

Federal Tax Return