



# Are you a U.S. Citizen or U.S. Resident investing abroad?

## You may need to re-evaluate your investment strategy.

### **Investing abroad is complicated for U.S. tax purposes.**

U.S. Citizens and U.S. Permanent Residents need to be aware of the U.S. tax ramifications of investing in non-U.S. mutual-type funds abroad, and seriously consider avoiding these investments. By understanding the tax and reporting cost issues associated with these investments, referred to as Passive Foreign Investment Companies (PFICs), American investors can make better decisions when managing their wealth globally.

### **What is a PFIC?**

When it comes to taxes, PFICs are extremely punitive. A U.S. incorporated mutual fund invested in European stocks that is held for more than one year will generally be taxed at the low U.S. long-term capital gain tax rates of 0%-20% on disposition, while a nearly identical fund listed and held outside the U.S. becomes subject to heavy-handed PFIC taxation, potentially counting all income (including capital gains) as ordinary income and automatically tax it at the top individual tax rate (up to 39.6%). Some unwary investors have realized total tax and related costs on PFIC investments at over 50%!

Because PFIC sounds like something highly unusual and specialized, many unsuspecting taxpayers make the mistake of assuming that they don't own any. In reality, the PFIC is not so exotic. For example, investments as simple as pooled fund investments that are registered outside of the United States are probably PFICs. These investments could include mutual funds, hedge funds or even insurance products. Certain non-U.S. pension plans can also fall under PFIC rules, unless the plan is recognized as exempt due to an income tax treaty that is in force between the U.S. and the plan's host country. Non-U.S. Trusts may be subject to PFIC taxation and reporting rules as well.

### **Reporting rules for PFICs make non-U.S. mutual fund investments even less attractive.**

The bad news for U.S. Citizens and U.S. Permanent Residents holding PFICs doesn't end with the taxation concerns. Adding to the complication of owning a PFIC is the complex task of abiding by IRS reporting rules. For example, IRS Form 8621 must now be filed EVERY year for each separate PFIC. Certain elections can be made in the first year that the PFIC is owned to reduce the punitive tax effect. Failure to make an election timely may result in dire tax consequences. Further adding to the reporting burden, IRS Form 8621 has to be filed even when a U.S. Citizen or U.S. Permanent Resident is otherwise under the tax return filing limit and not required to file a tax return.

In addition, IRS Form 8938 must also be filed EVERY year to report the value of all specified foreign financial assets. It would not take long to wind up with a significant



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tax preparation bill, no matter how much or how little the foreign investments are worth or how well they have performed.

## PFIC reporting is not optional.

Legislation regarding investments abroad has gone beyond self-reporting of PFICs, non-U.S. bank and brokerage accounts and other foreign-held financial assets. It requires many “foreign financial institutions” to report on assets held by U.S. Citizens and U.S. Permanent Residents. This information is now being reported to the IRS. Industry observers have seen nearly universal compliance of this law by banks, brokerages, insurance companies and mutual funds around the world, largely due to the severe sanctions that the law imposes on non-compliant institutions.

## What does this mean to you?

If you are an American investing in PFICs or you have a foreign financial asset or foreign trust, you must assume that the IRS has access to information about your holdings in foreign financial institutions. The IRS will cross-reference your Forms 8621 and 8938 to determine whether or not your PFIC investments have been properly reported and your tax correctly calculated and paid. Not filing has the potential to open you up to a tax audit, costly compliance filings and penalties or even prosecution for tax fraud. It's important to have an accountant who knows and understands the complexities of PFIC-related filing to assure proper understanding of the tax consequences and compliance with the reporting requirements.

Many accountants without international tax experience can easily overlook and fail to request information on investments held abroad. The International Tax Team at Kerkering Barberio has a wealth of experience providing personalized tax consulting and compliance services to clients who are U.S. Citizens and U.S. Permanent Residents in all parts of the world, as well as non-U.S. residents seeking personal or business tax advice when relocating to the United States.

To discuss your international tax and financial planning needs, contact **Phoebe Trumpler, CPA** at (941) 365-4617.

**Kerkering, Barberio & Co., CPAs** has been a part of the Tampa Bay community for over 40 years, and is one of Southwest Florida's largest independent CPA firms. Providing a variety of tax, audit and accounting services to businesses and individuals, KB brings together the best people, quality services and innovative products to assist clients in achieving their personal, business and financial goals.



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## MEET THE ACCOUNTANT

### Phoebe Trumpler, CPA

*Phoebe Trumpler, CPA joined Kerkering Barberio in 2005 and was admitted as a shareholder in 2016. Ms. Trumpler's primary practice is in International Tax, providing consulting, tax planning and preparation of U.S. tax returns for U.S. citizens and tax residents who have international income and investments. She assists individuals with offshore tax compliance issues related to Foreign Bank Account Reports (FBAR) and the Foreign Account Tax Compliance Act (FATCA). She also works with high net worth individuals who have only US income and accounts and assists them with tax planning and tax preparation needs.*