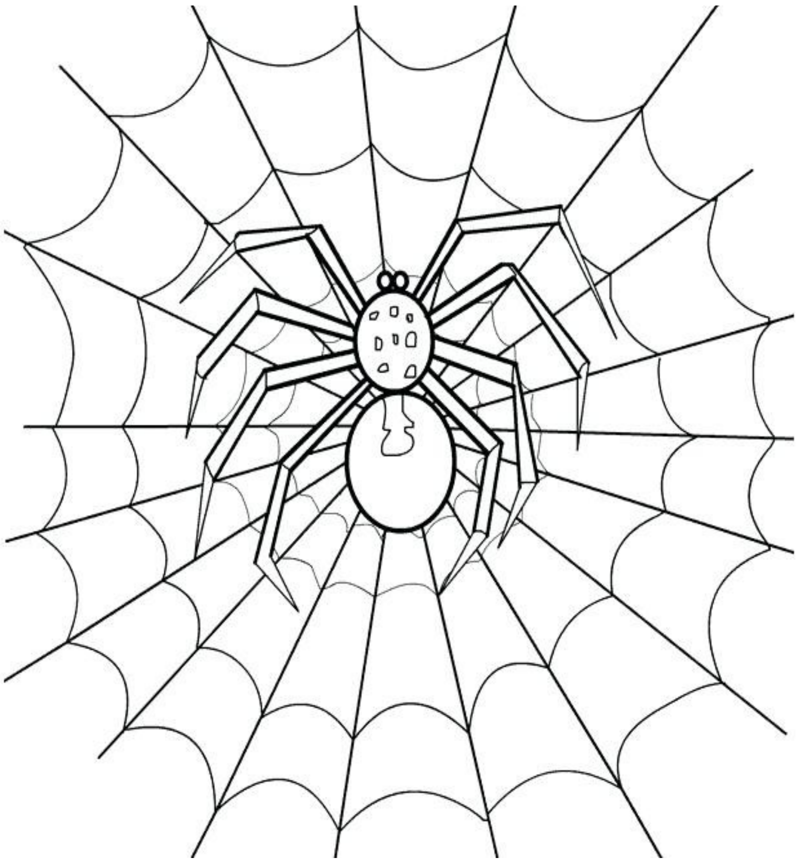
[EWP & Compliance Simplifier-Part 2]



International Tax Planning & Compliance Simplifier—Part 2

EWP (Expanded Worldwide Planning) and Compliance Simplifier

Private Placement Life Insurance (PPLI) in Action
Inside a Deadly Spider Web Structure

Depending on the planning needs of international families, two types of trusts are generally used, **Foreign Grantor Trust and Foreign Non-Grantor Trust**. These trusts can accomplish some of the aims of the six principles of EWP, but they can do nothing in terms of tax efficiency. For this a trust must own a properly structured PPLI policy. An EWP structure uses ***the six principles of EWP*** to give families the optimum amount of tax efficiency, privacy, and asset protection.

Foreign Grantor Trusts

A foreign trust is considered a grantor trust for U.S. income tax purposes when a U.S. grantor makes a gratuitous transfer to a foreign trust that has one or more U.S. beneficiaries or potential beneficiaries of any portion of the trust. The trustee of a foreign grantor trust with a U.S. owner is required to file Form 3520-A, Annual Information Return of Foreign Trust with U.S. Owner, with the IRS each year. Such form includes an accounting of the trust's activities for the year.

The Form 3520-A is due on March 15th and a six-month extension may be requested.

The trustee should also provide a "Foreign Grantor Trust Owner Statement" to each U.S. owner of a portion of the trust and a "Foreign Grantor Trust Beneficiary Statement" to each U.S. beneficiary who received a distribution during the taxable year.

The U.S. owner of the foreign grantor trust is subject to U.S. income tax on the portion of the trust income he or she is considered to own. In addition to the Form 3520-A, the owner must file a Form 3520, Annual Return to Report Transactions with Foreign Trusts and Receipt of Certain Foreign Gifts, to report any transfers to the foreign trust. Form 3520 must also be filed each year to report ownership of the foreign trust even if no transfer is made. Form 3520 is required to be filed by the due date of the individual's Form 1040 including extensions.

U.S. beneficiaries of a foreign grantor trust who receive any distribution during the taxable year must also file Form 3520 to disclose the amount and source of the distribution. In addition, the Form 3520 discloses the amount of taxable income that is includible on his or her income tax return. The U.S. beneficiary is also required to disclose the fact that a distribution was received on Form 1040, Schedule B, Part III.

Foreign Non-Grantor Trusts

Foreign non-grantor trusts generally are not subject to U.S. income tax unless the trust earns U.S. source or effectively connected income. Such income is taxed at graduated rates applicable to domestic trusts. Depending upon the investments that the trust holds as well as treaty considerations, the Trusts may be subject to non-resident withholding. Foreign information disclosures may be required as well.

The trustee should provide a Foreign Non-Grantor Trust Beneficiary Statement to a U.S. recipient that received a distribution which reports the amount of the distribution as well as a breakdown of the character of the income. The U.S. beneficiary is required to report the distribution received on Form 3520. In addition, the U.S. beneficiary must pay income tax on the current year trust income included in the distribution and may also be subject to an additional tax ("throwback tax") to the extent the distribution includes undistributed income from a prior year, termed undistributed net income (UNI). Further, in order to deter trusts that do not distribute income currently, an interest charge may be imposed.

Don't Trust in Trusts Alone

The strands that form a spider's web are sticky, and cling to you when touched. Likewise, a Spider Web Structure clings to tax authorities in very unwelcomed ways and binds you and your family to them through the overcomplication, confusion, and uncertainty of the asset structure.

We have chosen a ***Spider Web Structure*** that involves non-U.S. persons, who are neither U.S. citizens nor residents of the U.S.(NCNR). These families have both U.S. beneficiaries and non-U.S. beneficiaries, and have created two Foreign Corporations (FC). The Spider Web Structure begins simply enough, but as you will read, the ending is not so simple.

The trustees of the Foreign Grantor Trust (FGT) then created a second Foreign Corporation, which would own only non-U.S.-*situs* assets. The original FC would own only U.S. securities. The non-U.S. portfolio assets owned by the second FC would be earmarked to benefit solely non-U.S. persons as trust beneficiaries after the death of the NCNR. The U.S. portfolio assets owned by the existing FC would be earmarked for the U.S. beneficiaries.

There would be no U.S. estate tax on the non-US assets owned by the second FC. A retroactive check-the-box election could be filed for this second FC effective on the day before the NCNR's death.

Some US advisors advocate relying exclusively on entity structuring to convert a single FC into a multi-tier FC structure involving at least three FCs. Prior to the NCNR's death, the trustees of the NCNR's FGT would create two FCs. These two FCs would then together equally own the shares of a third lower-tier FC.

The US portfolio assets would be owned by the lower-tier FC. Following the death of the NCNR, the lower- and upper-tier FCs would be deemed liquidated for US tax purposes (by filing check-the-box elections) in a carefully scripted sequence as follows.

1. First, the upper-tier FCs would each file a check-the-box election for the lower-tier FC, effective one day prior to the death of the NCNR. This results in a taxable liquidation of the lower-tier FC without current US income tax on the historical pre-liquidation unrealised appreciation inside the FC. However, the upper-tier FCs' basis in the underlying US securities held by the former lower-tier FC will equal the FMV of such assets on the date of the deemed liquidation of the lower-tier FC.
2. Second, two days after the NCNR's death, both upper-tier FCs will make simultaneous check-the-box elections. The inside basis of the US portfolio assets previously held by the lower-tier FC prior to its deemed taxable liquidation would be stepped up or down to the FMV of such assets on the day after the death of the NCNR.

Now you understand why we call it a Spider Web Structure? In reading through this structure, do you get an eerie feeling that something might go wrong if something unexpected happens in the web? Perhaps these check-the-box elections might not be done in precisely this manner? Do you think we have an alternative? You are right!

PPLI: An Elegant Solution

An EWP structure is easily produced if the FNGT purchases a PPLI policy none of the above convoluted planning of the Spider Web Structure need occur. The PPLI structure satisfies the needs of both the U.S. beneficiaries and the non-U.S. beneficiaries, as assets in the policy can be located in any jurisdiction worldwide, and distributions can be made to both sets of beneficiaries in a properly structured policy without any taxation.

Once investments are part of a properly constructed PPLI policy none of the following are treated as taxable income:

- The income and investment returns inside the policy;
- Withdrawals up to premium;
- Policy loans, and;
- Death benefit proceeds.

Pre-immigration Planning

The strategy of funding a FNGT with PPLI is even more successful when applied prospectively, prior to the accumulation of any UNI in the trust, for example before a non-U.S. person establishes U.S. residency. By funding the FNGT with PPLI when the trust is first established, U.S. beneficiaries can remove UNI complications altogether. All the assets that are placed in this PPLI policy are effectively placed outside the U.S. tax system, and can be passed onto beneficiaries tax-free. Timing is crucial for this PPLI structure to be the most effective, as it needs to be established before the U.S. person has entered the U.S. tax system.

At the Heart of EWP Is PPLI

Why engage in complex trust and entity planning that just produces overcomplication, confusion, and uncertainty--yes, Spider Web Structures? You can definitely accomplish much more with a more simple and straightforward EWP Structure that uses PPLI as its core element. We invite you to ***inquire today*** to find out how we have helped families worldwide achieve privacy, tax efficiency, asset protection, and, of course, compliance simplification.

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