PKF PERSPECTIVES

INFORMATION FOR ALIENS DEPARTING THE U.S.

... Leo Parmegiani, CPA

As an aftermath to the terrorist attacks on the United States, immigration laws have become the focus of close scrutiny by U.S. authorities. In connection with this scrutiny is the examination of not only how a person has entered the country but also whether the person is fully compliant with U.S. law while present. Compliance includes meeting all the conditions of a particular visa status, not remaining beyond the allowable period, and the filing of all proper documents. These documents include, but are not limited to, tax forms and returns which are required not only to report income but also to provide the IRS with immigration and financial information and tax treaty benefits disclosure. Foreign nationals, now more than ever, must pay close attention to proper tax reporting or jeopardize their visa status.

Tax Requirements

Foreign nationals who are present in the U.S. are generally required to file U.S. Federal and State income tax returns, especially if they are present for at least 183 days during any calendar year or if they are working in the U.S. U.S. law taxes non-resident aliens (NRAs) on all personal service income that is *"earned"* in the U.S. at the same graduated rates applied to U.S. citizens and residents. Other U.S. source income that is of a more passive nature, such as interest and dividends is taxed at a flat 30 percent. NRAs generally must file U.S. returns if they are working in the U.S. even if they are exempt from tax by virtue of an income tax treaty with the NRA's home country.

NRAs become "residents" for tax purposes if they successfully obtain permanent residency status (a green card) or are present in the U.S. for at least 183 days during the current year or 183 days over a 3 year lookback which counts all days present in the current year, 1/3 of the days present during the first preceding year and 1/6 of the days present during the second preceding year. If the mechanical days present test is met, it is likely that an NRA would become a resident for tax purposes. In such case, he or she would be taxed on their worldwide income regardless of source. Resident aliens (RAs) generally have the same filing obligations as U.S. citizens but in the year of arrival, a special "Dual Status" return which splits the tax year into two periods is required.

Sailing Permits – Year of Departure

In general, unless an exception applies, foreign nationals who have been working in the United Sates are required to obtain a "Sailing Permit and Certificate of Compliance" from a local office of the IRS district in which they are employed before each departure from the United States. In effect, this is an information return designed to provide The IRS with sufficient data to determine whether the U.S. government is at risk of losing tax revenue by allowing the individual to depart without payment of tax.

Aliens should not leave the United States or any of its possessions without getting a Certificate of Compliance from the local IRS District Director on Form 1040-C or Form 2063, U.S. Departing Alien Income Tax Statement, unless one of the following exceptions applies:

- You are a representative of a foreign government who holds a diplomatic passport; a member of the representative's household;
- You are a student, industrial trainee, or exchange visitor, or the spouse or child of such an individual. To qualify for this exception, you must have an F-1, F-2, H-3, H-4, J-1, J-2 or Q visa. Additionally, you must not have received any income from sources in the United States **other than**:
  - Allowances covering expenses incident to your study or training in the United States (including expenses for travel, maintenance, and tuition).
  - The value of any services or accommodations furnished incident to such study or training.
  - Income from employment authorized under U.S. immigration laws.

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DEDUCTING WORLD TRADE CENTER DISASTER LOSSES

... Joseph V. Bencivenga, CPA

In response to the September 11, 2001 terrorist attack on the World Trade Center and on the Pentagon, the President declared the five counties of New York City and Arlington County in Virginia disaster areas. PKF has already issued a special report in its last edition of ***PKF Perspectives*** on relief granted for the filing of tax returns and meeting other tax obligations. In this issue PKF addresses the subject of disaster losses stemming from the attack.

In general, losses attributable to a presidentially declared disaster are deductible at the option of the taxpayer either in the year the loss is sustained **or** in the preceding tax year. In making the decision as to the year of deduction, one has to assess which course of action makes the most sense, from a tax and a cash flow standpoint.

The overriding issue is to determine whether a deductible loss has been incurred.

- First, in general, the loss has to be limited to the lesser of (a) the taxpayer's adjusted basis in the property, or (b) the loss in value as a result of the event. *For losses in a business where the property is totally destroyed, a special rule applies allowing the taxpayer to use the adjusted basis in the property for determining the loss even when the loss in value is less than its adjusted basis.*

- Second, the loss has to be a real loss, which is to say that it has to be a loss that has not been recovered by insurance or some other compensation.

For example —

If business property with an adjusted basis of $100,000 and a fair market value of $90,000 were totally destroyed and the taxpayer recovered $75,000 from insurance, the allowable loss would be $25,000, the adjusted basis in the property, $100,000, less the $75,000 insurance recovery. Same facts, but if the structure had a fair value of $180,000, the loss would still be limited to $25,000,the lesser of adjusted basis or loss in value, less the $75,000 insurance recovery. **Note that it is not just structures that are eligible for loss deduction; loss of inventory also qualifies.**

Another aspect to keep in mind is that, in general, from the standpoint of an individual taxpayer, losses are either business related or they are personal. The type of loss determines how it is to be reported.

The World Trade Disaster on September 11, 2001 is a defining event far beyond the order of hurricanes, tornadoes and the like. One has to recall December 7, 1941, that *day of infamy* in the words of Franklin Delano Roosevelt, to find as many Americans killed in a single event. Indeed, it is a disaster of enormous proportions, where thousands of Americans were affected, and huge losses sustained. Many are asking what losses can be deducted.

The regulations issued by the IRS say, in general, that to be allowable as a deduction the loss must be evidenced by

> ***"...closed and completed transactions, fixed by identifiable events.... Only a bona fide loss is allowable. Substance and not mere form shall govern in determining a deductible loss."***

PKF cannot identify all situations that might involve deductible losses, but it can describe some general conditions that apply in these situations.

For example —

If a business has been abandoned as a consequence of the collapse of the World Trade Center Towers or surrounding buildings, related losses to the business property or inventories that can be documented would be deductible.

◆***Observation: The taxpayer has to prove the amount of loss. The fact that records might have been lost in the disaster does not preclude a loss deduction. In this situation, the IRS will more than likely accept reconstructed records but, as one might expect, such records would be subject to greater scrutiny.***

An obvious question is whether a loss can be deducted for lost revenue or goodwill. The answer to most questions in this area of disaster losses depends on facts and circumstances, under applicable law and regulations. Losses have to derived from closed and completed transactions. On that score, lost business would fail to qualify, notwithstanding that the lost business is the direct result of the disaster.

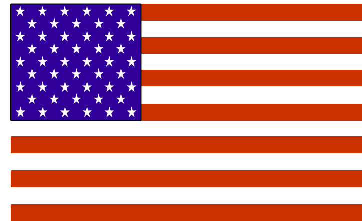
On the question of goodwill, the first issue is the amount of the goodwill and whether it resulted from a closed and completed transaction. In most cases, the goodwill of a business is an off-the-books intangible asset not resulting from a closed and completed transaction. Thus, in this case, goodwill would not constitute a deductible item. There are many situations, however, where a company bought another business in a way that resulted in the recognition of goodwill for tax purposes. Assuming other conditions can be satisfied here, there might be an opportunity for a deductible loss, if the goodwill of the acquired business has been permanently impaired.

Disaster losses sustained in a business would generally be deductible as ordinary losses but this depends on the gains, if any, that the business might have on the sale or disposition of other business property.

Regarding the manner in which losses can be deducted, it depends on the type of loss (personal casualty loss versus a business-related disaster loss). Casualty losses are deductible as itemized deductions subject to a $100 per event limitation but only when the amount exceeds ten percent of adjusted gross income. ***Since the taxpayer is eligible to choose the year when such a loss would be deducted (i.e., this year or last year), then, ignoring other factors, he or she would want to choose the year with the lower adjusted gross income as the year for such a deduction.***

Let us say that the taxpayer owned an apartment in the immediate vicinity of the disaster and the fallout in the form of dust and debris made the apartment uninhabitable, to say nothing of the thousands of dollars the taxpayer had to spend on the clean up; the apartment was not used for business. The loss here may be deductible as a casualty loss. Of course, to the extent that some of the loss may be compensated by insurance, then the amount of the loss to be deducted would have to be reduced by the amount recovered.

Sooner or later Americans will recover from the shock of the events of September 11. As part of the recovery process, taxpayers that have been affected need to focus on minimizing the losses through tax recoveries and other aid that is available. PKF has focused on the tax side of the 'recovery' equation. Taxpayers with situations of special complexity should always seek professional advice to assure that the tax benefits to which they are entitled are obtained at the earlier opportunity.



This article discusses the tax ramifications of casualty and disaster losses. Those who have sustained disaster losses should be aware that assistance might be available in the form of loans or grants from the Federal, State and local governments. At the Federal level, for information as to what aid might be available, you should call the Federal Emergency. Management Agency (FEMA) 800-462-9029 or visit the agency website at www.fema.gov.

Information for Aliens Departing the U.S.

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How to Obtain the Certificate

To get a compliance certificate, aliens must go to the local IRS office at least two weeks before departing the United States and file either Form 2063 or Form 1040-C, and any other tax returns that have not been filed as required. The certificate may not be issued more than 30 days before departure.

Be prepared to furnish anticipated date of departure and the following records/documents if they apply:

1. A valid passport with your alien registration card or visa.
2. Copies of your U.S. income tax returns filed for the past two years.
3. Receipts for income taxes paid on these returns.
4. Receipts, bank records, canceled checks, and other documents that prove your deductions, business expenses, and dependents claimed on the returns.
5. A statement from each employer you worked for this year showing wages paid and tax withheld.
6. Proof of any payments of estimated tax for the past year and the current year.
7. Documents showing any gain or loss from the sale of personal property.
8. Documents concerning scholarship or fellowship grants.
9. Documents indicating qualification for special tax treaty benefits.

Departing aliens should be aware of this sailing permit requirement. Although technically necessary, enforcement of these returns has been relaxed over the last 10 years with increased international travel and post cold war sentiment. ***However, times have changed and departing aliens should at least be in a position to know exactly what their tax liability is. One simple way to avoid the compliance certificate route is to obtain a letter from one's employer stating that the employer guarantees all taxes owed.*** This will satisfy the IRS.

If you would like more information on this topic, feel free to contact a PKF tax advisor.

In the Words of ...

Arthur C. Clarke: ***The best measure of a man's honesty isn't his income tax return. It's the zero adjust on his bathroom scale.***

Items in this publication should not be considered official statements of position, nor advice for individuals or organizations without consulting a tax advisor. For more information, please contact Howard Pell or Leo Parmegiani at:

PKF

Certified Public Accountants
A Professional Corporation

420 Lexington Avenue
New York, NY 10170
Telephone: (212) 867-8000
Telefax: (212) 687-4346
E-mail: info@pkfny.com

A copy of this and prior issues of **PKF Perspectives** can be found on our web page: www.pkfnewyork.com.