

## **Investment Account Considerations for US Expats**

June 2015

Dealing with financial matters has become increasingly difficult for US citizens living outside the USA over the last few years as a result of what is called FATCA (Foreign Account Tax Compliance Act), which has led to both US and non-US financial institutions being reluctant to deal with American expats. In our financial planning practice we receive many enquiries from US expats regarding how best to deal with banking and investment accounts, especially US retirement accounts, and whether offshore or non-US investment accounts are a good idea for US expats.

I've discussed difficulties in managing US retirement accounts for expats in another article so I won't repeat that information here except to point out the pitfalls of using a US address on a financial account when actually not a US resident. Many US expats get around the issue of their brokerage firm wanting to close or freeze non-resident accounts by using a US address on the account. This address may be a mail forwarding service or perhaps the address of a friend or relative, or of a property they own but do not live in. There are a couple of things to be aware of with respect to this:

First of all, a number of brokerage firms track IP addresses when their clients log into their accounts on line. These IP addresses show where the person is located so if someone is consistently logging in from abroad then their US financial firm may at some point ask them to prove that they actually do live at the address they use on their account.

The second issue arises if the address being used is in a US state that has an income tax. If this is the case and there are taxable withdrawals from a retirement account or income from a taxable investment account then this will be reported to the state of record on the account on a 1099 form at the end of the year. If taxes are not being filed in that state, since the account owner is actually not a resident, then the account owner may receive a letter from the state tax board wondering why state income tax isn't being paid on the amounts reported on the 1099. Frankly, a better solution is to find a brokerage firm or financial advisor that will not require a client to lie about their address of residency in order to have an account with them.

What about maintaining investment accounts in the country of residency rather than the USA? This may be a good alternative if the brokerage firms in that country will deal with US citizens and if the products offered and fees charged are attractive; but there are a number of issues to consider:

First of all: Would the account be protected by insurance against the default of the financial institution? In the USA we have SIPC insurance up to \$500,000 for brokerage accounts (and usually private insurance on amounts greater than that), and FDIC insurance of \$250,000 for bank accounts. Most developed countries have a similar form of protection but amounts vary and are often less than in the USA. Many developing countries do not have such protection at all.

Secondly: What investment or banking products are available? The USA has by far the broadest range of investment products available through financial institutions. Even in many developed countries investment products are often heavily weighted to mutual funds or insurance products. While mutual funds can be appropriate investments for many people, there are a large variety of other investment products out there that can help diversify a portfolio and may provide better solutions to specific investor needs. Also certain investment products, such as non-US mutual funds, require additional US tax reporting and may be taxed in an unfavorable manner.

Thirdly: What are the fees associated with the account and the investment products and are these fees transparent? The USA has a very competitive financial marketplace and therefore fees tend to be lower than in many other countries. As an example, trading fees at a US discount brokerage are typically a few dollars per trade whereas at an offshore brokerage firm in Luxembourg that describes itself as a "discount" broker trading costs are between \$20 and \$60 per trade. Also offshore non-US mutual funds typically have higher management fees than US funds. Life insurance investment products are common in the offshore world and these often have a lock-up period and surrender charges to withdraw funds, as well as high account fees that are sometimes not explicitly stated.

Yet another point: When dealing with a non-US financial advisor or offshore investment company what recourse does the client have against such issues as misappropriation of funds or recommendation of unsuitable investments or hidden fees? In the USA and in most developed financial markets there are investor protection laws and a regulatory body that enforces these laws as well as a robust legal system through which a client can seek redress. There are licensing procedures for advisors and laws pertaining to marketing of investment products and oversight of such products through registration. Such investor protection is not available in many less-developed and lightly regulated financial markets.

Finally: US citizens and Green Card holders need to declare their non-US financial accounts over \$10,000 in aggregate to the Treasury department

each year in what is known as FBAR filing and they may need to complete IRS form 8938 as well. Worldwide income is subject to tax in the USA no matter the country of residency and should be declared on US tax forms (although in practice it may not actually be taxed in the USA if there is a tax treaty with the country of residency). So a non-US investment account for someone who wants to remain US tax-compliant may be more of a liability than a benefit.

Everyone's situation is different, and for US expats living in developed financial market countries investing locally may still be the best solution; but for expats in less developed countries we strongly advise considering the points mentioned above.

Tom Zachystal, CFA, CFP™

*Tom Zachystal is President of Individual Asset Management, a Registered Investment Advisor specializing in investment management and financial planning for expatriates.*

**This article is for informational purposes only; it is not intended to offer advice or guidance on legal, tax, or investment matters. Such advice can be given only with full understanding of a person's specific situation.**