Week3

Finance

Finance and accounting al affiliation Strategy to optimize foreign tax credits

Foreign subsidiaries tax liability can be reduced by adopting the following strategies; apply various investment tools e. g. using an option spread transaction can help reduce tax liability of the parent company by increasing credit limit for foreign income tax. A company can also take advantage of IRS §904 by using transactions of offshore financing, this converts passive income to active non U. S income thus able to claim foreign tax credit. This is an example of income reclassification, (Foreign Tax Credit, 2014)

Abuse of foreign tax credits

Most likely abuse of foreign tax credit included the following; assets generating income stream that is subjected to foreign withholding tax. Attempt to use laps between foreign tax law and U. S to effectively duplicate tax benefits. The treasury should address this lop holes by use of existing laws and by legislation of bylaws to cub this practice. (Albrecht, Albrecht, 2008).

A U. S citizen can reduce or minimize U. S. tax obligations by claiming tax credit on foreign taxes on income. This is subjected to the following condition; the maximum tax credit payable must not exceed the amount of tax that would be payable if this income tax was taxed using domestic income tax rate. Any excess tax paid to a foreign county is not claimable. For example if a U. S citizen X earns $9, 000 foreign annual income and this is the only of taxable income for X. And x had paid 800 as tax on this income. His domestic tax liability will be 900 less 800 tax credit.

Argument for Elimination tax exemptions for U. S Taxpayers on income generated from abroad

The government should maximize its tax revenue by not allowing any tax credit to its tax payers working abroad. This will seal lop holes that currently exist on this legislation.

For example if a U. S citizen X earns $9, 000 foreign annual income and this is the only of taxable income for X. And x had paid 800 as tax on this income. His domestic tax liability will be 900 less 800 tax credit. However, is this tax credit is eliminated; the government will earn an additional 800.

Argument against Elimination tax exemptions for U. S Taxpayers on income generated from abroad

This will lead to double taxation of taxpayers hence exploitation by the government thus discouraging foreign employment. I. e. X (above illustration) will pay 1700 as tax.

Reference

Foreign Tax Credit (2014) IRS, retrieved from http://www. irs. gov/Individuals/International-Taxpayers/Foreign-Tax-Credit

Albrecht, C. & Albrecht, C. (2008). The nature of financial statement fraud. Internal Auditing, 23(4), 22-27.