

Fall 1996

To All of Our Valued Clients and Friends:

We are pleased to be able to send you our Fall newsletter. Our topics for this newsletter are as follows:

- Our service - 1996 Individual tax return
- IRS Individual taxpayer identification number(ITIN)
- Exchange rate gain on sale of foreign residence

Our Services

- The time to file our individual tax returns is just around the corner. We hope that you will consider us in preparing your tax returns. Kakimoto and Co., LLP has the capability of preparing income tax returns for personnel who have arrived or departed the United States (dual status tax returns), who have transferred job locations within the United States (multiple state tax returns), or who reside in any state . We specialize in the preparation of individual income tax returns for Japanese nationals who are assigned to U.S. offices for short or long-term assignments. Each income tax return is prepared with consideration given to any tax benefits provided by the Internal Revenue Code or the United States - Japan income tax treaty. Many of our professional staff are fluent in Japanese. Our fees are generally 30 % to 40% less than those charged by most Big 6 accounting firms.
- We are still offering the Peachtree promotional service to our valued clients and any new clients. We will provide a free demonstration of the Peachtree accounting software, and we will be more than happy to discuss your Company's accounting needs as our service to you. There is no charge for the demonstration and initial meeting. Please call to make an appointment at your earliest convenience.

If you are interested or have any questions, please call Gerald W. Kakimoto or Takako Kondo at (310) 715-9100 or fax your requests to (310) 715-9830.

Please feel free to call us for the Japanese version of this newsletter.

All of your support is greatly appreciated.

Kakimoto and Co., LLP

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OUR SERVICE - 1996 INDIVIDUAL TAX RETURN

Kakimoto and Co., LLP provides excellent accounting, tax and management consulting services. Our professional staff possess the technical experience, knowledge and resources to tackle complex international tax issues and difficult accounting areas, in addition to providing a wide range of other diversified services. Our commitment to quality and personal approach to services has resulted in the growth of our client base to include small companies as well as multinational corporations in a broad range of industries.

The season for individual tax returns is drawing near. For the individual and corporate tax compliance requirements, our entire staff, consisting of approximately 20 professionals, participates in the preparation of the tax returns. We have the capability of preparing tax returns for any state; tax returns are processed in our office using the same advanced software used by many of the Big 6 accounting firms.

We specialize in the preparation of individual income tax returns for Japanese foreign nationals who are assigned to U.S. offices for short- or long-term durations. We are also available to consult with you as to your tax requirements and planning; each return is prepared on an individual basis with consideration given to any tax benefits from the U.S.- Japan tax treaty, as well as U.S. income tax laws and regulations. Of our current clients, several are former Big 6 clients who are taking advantage of our competitive fees which are generally 30 to 40% less than those charged by most Big 6 accounting firms .

IRS INDIVIDUAL TAXPAYER IDENTIFICATION NUMBER (ITIN)

The Internal Revenue Service (IRS) has announced regulations which allow an individual to obtain an "IRS Individual Tax Identification Number (ITIN)" when an individual is unable to receive a social security number (SSN). An ITIN is a nine-digit number issued by the IRS to individuals who are required to have a U.S. taxpayer identification number but who do not have, and are not eligible to obtain, a social security number. This regulation is effective July 1, 1996. ITIN's will be required for the filing of 1996 income tax returns.

There have been occasions where a newly arrived Japanese employee transferred from the parent company in Japan has had difficulties in obtaining social security numbers for a spouse and/or a dependent from the Social Security Administration due to the spouse and/or dependent not having legal authorization to work in the U.S. However, a taxpayer is required by the IRS to report a taxpayer identification number for a spouse and/or dependent on the personal income tax return.

An individual who is not eligible to obtain a SSN and whose taxpayer identification number is required to be furnished to the IRS must apply for an ITIN on Form W-7. Examples of those who must apply are as follows:

Nonresident alien individuals not eligible for a SSN who are required to file a U.S. tax return or who are filing a U.S. tax return to claim a refund.

Nonresident alien individuals not eligible for a SSN who elect to file a joint U.S. tax return with a spouse who is a citizen or resident.

U.S. alien residents who file U.S. tax returns and who are not eligible for a SSN.

Alien individuals claimed as dependents on U.S. tax returns and who unable or not eligible to obtain a SSN.

Alien individuals claimed as spouses for exemptions on U.S. tax returns and who are not eligible to obtain a SSN.

You should not file Form W-7 if you have a SSN or you are eligible to obtain a SSN. U.S. citizens, nationals, and individuals that have been lawfully admitted for permanent residence or U.S. employment are eligible to obtain a SSN.

The application to obtain an ITIN can be made by mail or in person at most IRS offices or U.S. consulate offices abroad. If filing Form W-7 in person original documents which substantiate the information on the Form W-7 must be provided. Examples of acceptable documents include an original passport, driver's license, birth certificate, identity card, or U.S. immigration documents. If you apply by mail, Form W-7 should be mailed along with the certified supporting documents to:

Internal Revenue Service
Philadelphia Service Center
ITIN Unit
P.O. Box 447
Bensalem, PA 19020

Copies of supporting documents can only be certified by the issuing agency of the documentation. Therefore, it may be a difficult process to apply by mail.

EXCHANGE RATE GAIN ON SALE OF FOREIGN RESIDENCE

Fluctuating exchange rates can add another level of complexity to calculating the capital gain on the sale of a foreign residence by United States taxpayers. A taxpayer that purchased a residence in Japan may want to reduce their capital gain by using the exchange rate on the date of sale to calculate both their cost basis and their selling price. However, the First Circuit Court recently ruled in *Quijano v US* that taxpayers must use the different exchange rates in effect when the home was purchased, when each capital improvement was made, and when the home was sold.

Example:

The purchase. While the taxpayer was in Japan, he acquired a home for 17,800,000 yen in December 1984. The exchange rate at the time was \$1.00 to 251.40 yen. The entire purchase price was financed through a mortgage loan in yen that was increased twice to a total of 19,690,000 yen as the taxpayer made capital improvements of 890,000 yen in June 1990 and 1,000,000 yen in January 1991. The condo was sold in May 1995 for 20,000,000 yen. The value of the dollar declined against the yen during this period so the exchange rate at the time of the sale was \$1.00 to 87.18 yen. That is, it took 164.22 less yen to buy a dollar when he sold the house compared to when he bought it.

Capital gain on the real estate sale. Both the Internal Revenue Service (IRS) and the taxpayer will agree that the 20,000,000 yen that the taxpayer received for the residence should be translated into U.S. dollars at the exchange rate at the time of sale. They will differ on the exchange rate to be used to calculate the dollar equivalent of the 19,690,000 yen basis in the

property, consisting of the 17,800,000 yen purchase price plus the two capital improvements totaling 1,890,000 yen. By using the higher rates in effect at the time of purchase (\$1.00 to 251.40 yen), when the first capital improvement was made (\$1.00 to 154.00 yen), and when the second capital improvement was made (\$1.00 to 134.00 yen), the Service calculates a gain of approximately \$145,000.00. By using the lower rate in effect of the time of the sale (\$1.00 to 87.18 yen), the taxpayers increase their basis and reduce the gain to approximately \$3,600.00. The \$141,400.00 represents unrealized foreign exchange loss due to the decline of the dollar against the yen.

The IRS will agree that the taxpayer suffered a loss on the mortgage transaction. Because the value of the dollar declined against the yen between the time of the purchase and the time of the sale, it took more dollars to pay off the mortgage than if the value of the dollar had stayed constant.

The problem for the taxpayer is that the loss on the mortgage transaction is not deductible because it was not incurred in a trade or business or a transaction that was entered into for profit. The taxpayer is also not allowed to combine the sale of the home and the mortgage transaction in determining the gain/loss on the sale of the home. The First Circuit Court has previously ruled that the borrowing and repayment of a mortgage loan is a separate transaction from the purchase and sale of a personal residence

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