

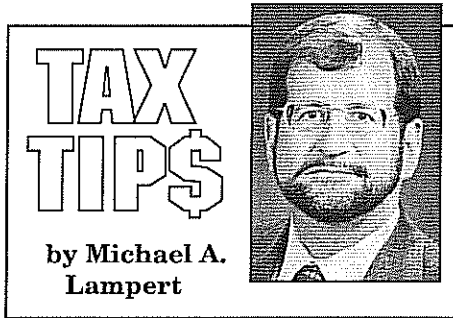
# Basics of estate and gift tax for non-citizens

Recently there has been a series of questions on the Elder Law Listserv regarding estate and gift taxes for non-citizens. Prior Tax Tip articles have addressed the reporting of undisclosed offshore financial accounts (see, e.g., Offshore financial accounts, IRS Voluntary Disclosure Initiative, "Round Two" in vol. XIX, no. 1, spring 2011, page 9). In addition, the summer 2011 Tax Tips column addressed accounts owned by foreigners, although that article emphasized which assets are and which are not U.S. situs assets.

The law regarding taxation of non-citizens is complex. The general rules are further complicated because the United States has tax treaties with certain other countries. The United States does not have tax treaties with all countries, and all tax treaties are not the same. In addition, some of the treaties address only some aspects of tax, such as income tax and not estate tax.

With that said, there are some general tax rules regarding non-U.S. citizens' estate and gift taxes of which elder lawyers should be aware. Many times a basic understanding of the law is all that is needed to address the issue, or to recognize that assistance is needed.

For estate and gift taxes, there are three categories of individual taxpayer: U.S. citizen, resident alien domiciliary (RAD) and non-resident alien domiciliary (NRAD). To determine domicile (residency) in close cases, get help. Why? The test to determine domicile for estate and gift taxes is different than for income tax, which has somewhat more clear tests of substantial presence and green card. For estate and gift tax, simply stated it is an intent by the NRAD to reside permanently in the United States, with various factors looked at to determine intent (e.g., U.S. "green card").



## *Who and what are subject to estate and gift tax?*

U.S. citizens and RADs are subject to estate and gift tax on their worldwide assets.

NRADs are taxed on gifts of U.S. situs assets. Most gifts of intangible U.S. assets are not taxed. Not considered U.S. situs are bank and brokerage accounts that are not U.S. trade or business accounts, and stock in U.S. corporations. The law regarding situs of partnerships and LLCs is not settled for estate tax purposes.

### **Trap #1**

The rules for what are U.S. situs assets for gift tax on NRADs are different than those for estate tax. NRADs may have estate tax inclusion of both tangible and intangible property in the U.S. life insurance on the life of a foreign person, U.S. non-business bank accounts and U.S. treasuries, and other portfolio debt obligations are generally not included.

### **Tip #1**

Always check to see if there is a tax treaty with the NRAD's country of citizenship. If so, special rules may apply, including rules specifying where an asset is deemed located (situs).

### **Exemption amount—how much?**

Citizens and RADs are entitled to the full estate tax exemption amount, indexed for inflation.

NRADs receive only an estate tax (not gift tax) exemption of \$60,000. This amount is *not* indexed for inflation.

**Reminder:** Check to see if a tax treaty changes the treatment.

### **Tip #2**

For an NRAD with a fair market value at death of U.S. situs assets in excess of \$60,000, a Form 706 NA is needed.

### **Trap #2**

Don't forget to determine prior lifetime gifts of U.S. situs assets. As with citizens, this can impact the remaining available exemption amount.

### **Trap #3**

U.S. citizens and long-term residents who relinquished their U.S. citizenship or ceased to be U.S. lawful permanent residents (green card holders) on or after June 17, 2008, and who meet specific average tax or net worth thresholds on the day prior to their expatriation are considered "covered expatriates" and are subject to expatriation tax (I.R.C. § 877A.)

U.S. citizens, domestic trusts and probably RADs who receive gifts or bequests after June 17, 2008, from covered expatriates may be subject to transfer tax under IRC § 2801.

### ***So the client says, "Who cares, what can the IRS do anyway?"***

The Internal Revenue Service may collect any unpaid estate tax from any person receiving a distribution of the decedent's property under transferee liability provisions of the Internal Revenue Code. In addition, there is also the general estate tax lien that automatically is applied at death.

### ***So, who can give to who (or is it whom?) and with what result?***

The following tables provide guidance:

**GIFT TAX**

From	To
U.S. citizen or RAD	citizen spouse <i>unlimited marital deduction</i> citizen, RAD or NRAD non-spouse <i>current annual exemption</i> <i>estate tax exemption (currently \$5.43 million)</i>
U.S. citizen or RAD	RAD or NRAD spouse <i>annual exemption \$145,000 or</i> <i>estate tax exemption (currently \$5.43 million)</i>
NRAD (U.S. situs property)	citizen spouse <i>unlimited marital deduction</i> citizen, RAD or NRAD non-spouse <i>current annual gift exemption amount of \$14,000</i> <i>no estate tax exemption</i>  <b>Note (and little Trap #4):</b> This NRAD grantor category is addressing U.S. situs property. While U.S. citizens and income tax residents need to report a receipt of a gift from an NRAD of non-U.S. situs property, there is generally no federal tax consequences of the gift.

**ESTATE TAX**

From	To
U.S. citizen or RAD	citizen spouse <i>unlimited marital deduction</i> citizen non-spouse and RAD and NRAD spouse and non-spouse <i>estate tax exemption (currently \$5.43 million)</i>  <b>Tip #3:</b> If there is a concern about exceeding the exemption amount to a non-citizen spouse, a qualified domestic trust (QDOT) can often be utilized. This allows deferral of the estate tax until the non-citizen spouse dies or the principal is paid out. There are many technical rules regarding QDOTs, but it is a viable planning alternative in appropriate circumstances.
NRAD (U.S. situs property)	citizen spouse <i>unlimited marital deduction</i> citizen non-spouse <i>\$60,000 exemption</i> RAD or NRAD spouse or non-spouse <i>\$60,000 exemption</i>

**What about portability?**

Using the deceased spouse unused exemption amount (DSUE), U.S. citizens and RADs may elect portability. NRADs generally cannot elect portability unless a treaty applies. Treaties might allow the use of the DSUE and even allow for a higher exemption amount for NRADs than the usual \$60,000. Careful consideration of the portability exemption must be made when utilizing a QDOT.

**Note:** The QDOT referred to above can also be utilized for NRAD gifts at death to a RAD or an NRAD spouse.

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