U.S. ESTATE AND GIFT TAX CONCEPTS

ITSG WORLD TAX CONFERENCE
MUNICH, GERMANY
NOVEMBER 2 - 4, 2016

Galia Antebi
Ruchelman P.L.L.C.
New York City
antebi@ruchelaw.com

U.S. Resident for Estate and Gift Tax Purposes

- Estate and gift tax apply to transfers made by a “resident” of the U.S.
- The tax is imposed on the donor who makes the gift or bequest, not the recipient
- The tax is based on value over a lifetime exemption
- “Resident” for these purposes means a U.S. citizen and any individual who has his “domicile” in the U.S. at the time of the gift or the time of death
- A person acquires a domicile in a place by living there with no definite present intention of moving away permanently

U.S. Resident for Estate and Gift Tax Purposes

- Living in the U.S. for even a brief period of time may be enough to establish domicile
- Residence without the requisite intention to remain indefinitely will not constitute domicile
- Once U.S. domicile established, it remains until a different domicile elsewhere is established – even after the person physically leaves the U.S.
  - Intention is a key feature to establish domicile, but not enough to change a domicile
  - Whenever there is doubt – there is no doubt…

U.S. Resident for Estate and Gift Tax Purposes

- Residence for estate and gift tax purposes is a subjective facts and circumstances test
  - May yield a result that differs from the result under the objective test for income tax purposes
  - In 1984, an objective test was adopted under the income tax
  - Prior to that time, the subjective tests applied to income tax
- Green card = permanent residence
  - Holder is presumed to have the requisite intent, but can prove otherwise based on facts and circumstances
  - Difficult burden of proof
- Query as to:
  - Effects on immigration status
  - Effects on “long term residents” – relinquishment of green card

Estate and Gift Treaties

- An individual can have only 1 domicile
- Two countries may view same person as domiciled in their country
- If a treaty is available the “tie breaker” may determine which governs
- The U.S. has over 65 income tax treaties but only 16 estate and gift tax treaties

Countries with Estate and Gift Treaties

- Australia
- Austria
- Canada*
- Denmark
- Finland
- France
- Germany
- Greece
- Ireland
- Italy
- Japan
- Netherlands
- Norway
- South Africa
- Switzerland
- United Kingdom

*Through the income tax treaty

U.S. Gift Tax on Nonresidents

- When a noncitizen, nonresident individual makes a gratuitous transfer during life, gift tax applies if:
  - The gifted property is situated in the U.S. and
  - The gifted property is real property or tangible personal property such as art, jewelry, automobiles
- Transfers of intangible property are not subject to gift tax
  - The term intangible property is defined for gift tax purposes only by examples, including stock, bonds, debt obligations, and bank deposits; cash is tangible property
  - In certain provisions relating to income tax, intangible property is defined as property for which value is determined by reference to the property's intangible elements rather than to the property's tangible form
  - Old rulings issued when the U.S. was on the gold standard, still lead to misunderstanding regarding wire transfers to banks in the U.S. and checks

U.S. Estate Tax on Nonresidents

- Common error frequently exists when real estate is owned
  - Real estate is transferred to a partnership and the partnership interest is gifted
  - Here, step transaction applies making the subject of the gift real property
  - Old and cold restructuring is honored
- Nonresident, non-citizen individuals are entitled to a $13,000 unified credit during lifetime – one credit covers estate and gift taxes
  - The credit shelters up to $60,000 of property transfers during life and death
  - Credit mechanism allows for exemption with progression
- Gift tax rate is graduated until $1.0 million
  - The aggregate tax is $345,000
  - Thereafter, a flat 40% tax applies

U.S. Estate Tax on Nonresidents

- When a noncitizen nonresident makes a transfer at death it is subject to tax if the property is situated in the U.S.
- Transfers of intangible property are subject to estate tax
- Unused unified credit applies to estate tax
  - Total credit claimed during life and at death cannot exceed $13,000
  - The credit shelters up to $60,000 of property transfers, whether given during life or at death
- The combined estate and gift tax rate is graduated for transfers during life and at death until $1.0 million is given
  - The aggregate tax is $345,000
  - Thereafter, a flat 40% tax applies

Taxable Base of Estate tax

- Noncitizen nonresident U.S. gross estate will generally not be allowed to deduct value of liabilities imposed on the property
  - Exception: non-recourse debt secured only by the property
- Deductions will be allowed only if worldwide gross estate and liabilities are disclosed, and only a pro rated portion based on assets

Fact Pattern

Family Members:

- Parents are residents of Country X in E.U. – 1st generation
- 4 children, all nationals of Country X in E.U. – 2nd generation:
  - 1 lives in Country X
  - 1 U.S. Green Card holder living in Country X
  - 1 U.S. Green Card holder living in the U.S.
  - 1 lives in the U.S. as a student on an F-1 visa
- 3 Grandchildren, all U.S. citizens – 3rd generation

Fact Pattern

Assets:

- Shares in a Country X company, held directly by 1st and 2nd generations

Transaction:

- An irrevocable trust is formed by the father for the benefit of his wife and the 2nd and 3rd generations
- Trust owns U.S. real property

U.S. Results

- Child holding green card and living in the U.S. presumed domiciled
- Child living in the U.S. on student visa likely is not domiciled
- Query as to the Green Card holder not living in the U.S.:
  - If viewed to be domiciled –
    - World-wide assets are subject to estate tax at death
    - Gift tax applies to inter-vivos transfers
    - $5.45 million of assets can be shielded by lifetime credit
  - If not viewed as domicile in the U.S.:
    - Only U.S. situs tangible and U.S. real property assets are subject to U.S. gift tax
    - All U.S. situs assets are subject to U.S. estate tax
    - Only $60,000 can be shielded
  - Estate tax treaty, if applicable, may effect result
- Is the Green Card holder a "long term resident"?
  - If answer is yes – can taking the position individual is not domiciled in the U.S. result in expatriation treatment? Expatriation tax is an income tax concept with an inheritance tax tail – not estate and gift tax
- U.S. real property in irrevocable trust is not subject to estate tax at father's death if father did not retain right to income or the right to control the beneficial enjoyment by others of trust income or assets

Reporting Under C.R.S.

- If Trust is resident in a C.R.S.-participating country:
  - Country X resident beneficiaries, as well as Country X resident settlor, and any C.R.S. participating country resident protector appointed to the Trust will be reported to their country of residence by the Trust
- If Trust is resident of the U.S. for C.R.S. purposes:
  - No reporting under C.R.S.
  - If Country X is a F.A.T.C.A. counter party with which the U.S. has a reciprocal I.G.A. in place, the U.S. will report U.S. source interest income earned by individuals on depository accounts and U.S. source interest and dividend earned on non-depository accounts
  - Non-U.S. entities are not looked through
- U.S. resident for C.R.S. purposes does not mean U.S. resident for income tax purposes
- Look through rule by non-U.S. financial institutions

ruchelman
corporate
international
taxation

NEW YORK
Ruchelman P.L.L.C.
Architects and Designers Building
150 East 58th Street, 22nd Floor
New York, New York 10155
Tel. 212-755-3333

TORONTO
Ruchelman P.L.L.C.
The Exchange Tower, P.O. Box 233
130 King Street West, Suite 2300
Toronto, Ontario M5X 1C8
Tel. 416-350-2026

Important Notice

This presentation is not intended to be legal advice. Reading these materials does not create an attorney-client relationship. The outcome of each case stands on its own merits.