

## U.S. Estate and Gift taxation of resident aliens and nonresident aliens — 2010–2012



Non-U.S. citizens, both resident and nonresident aliens, may be subject to U.S. estate and gift taxes. Whether in the United States indefinitely, for a long-term stay, or short-term assignment, the death of a non-U.S. citizen may have adverse U.S. estate tax consequences. Likewise, lifetime transfers by non-U.S. citizens may be subject to U.S. gift tax. This publication will provide an overview of the questions that must be addressed by non-U.S. citizens who live, work, or own property in the United States.

In 2001, the U.S. Congress passed legislation that gradually phased out the U.S. estate tax with a full repeal in the year 2010. In late 2010, Congress acted to retroactively reinstate the estate tax for 2010–2012, with a maximum tax rate of 35% and an expanded exemption amount of \$5 million for U.S. citizens and U.S. domiciliaries. However, under the new law, the exemption amount for non-U.S. domiciliaries remains at only \$60,000, unless increased by treaty. To mitigate the effect of the retroactive estate tax for decedents dying in 2010, the new law provided executors with the option of electing out of the estate tax in favor of a “carryover basis” in the decedent’s assets. Even if the executor elects out of estate tax and in favor of carryover basis for 2010, for the estates of U.S. citizens and certain U.S. residents, limited basis step-ups (of generally up to \$1,300,000 plus an additional \$3,000,000 for transfers to a surviving spouse) are available. However, a step-up of only \$60,000 (in place of the \$1,300,000) is available to the estates of non-U.S. persons.

**Please note that this publication reflects the current U.S. Estate and Gift tax rules, which are presently scheduled to expire after December 31, 2012.** If there is no intervening legislative change, as of January 1, 2013, the rules will revert to pre-2001 rules, which are not outlined in this publication.

## I. What should I consider when moving to the United States?

### Should I get a green card?

Obtaining a green card is one way to establish residency in the United States. Having a green card allows for easier travel into and out of the United States and will allow you to remain in the United States indefinitely. However, a green card will subject you to U.S. income tax on your worldwide income during the entire time that you hold the green card (even if you are living outside the United States), and it may subject you to U.S. estate and gift tax on your worldwide assets if you make gifts or die while holding the green card (see discussion below).

### What happens if I later give up my green card?

Surrendering your green card will cause you to be considered a nonresident alien for U.S. income tax purposes (assuming you do not spend substantial time in the United States after surrendering your green card and, therefore, become a U.S. resident under the substantial presence test). However, upon surrendering your green card, you will need to consider whether you are subject to the U.S. “exit tax.” U.S. law imposes a “mark-to-market” exit tax applicable to certain U.S. citizens and long-term green card holders who expatriate or relinquish their green cards after June 16, 2008 (a “covered expatriate”). The law also imposes a tax on U.S. citizens or residents who receive certain gifts or bequests from covered expatriates. A covered expatriate is a person who renounces U.S. citizenship or who relinquishes a green card after holding it during any portion of at least eight of the last 15 years and who (i) has an average annual net income tax liability for the five preceding years of more than \$145,000 (for 2010, adjusted annually; 2011 amount is \$147,000), (ii) has a net worth of \$2,000,000 or more, or (iii) fails to certify compliance with U.S. tax obligations for the prior five years. Under the exit tax, covered expatriates are treated as having sold all of their worldwide property in a fully taxable transaction on the day before their expatriation date. Covered expatriates must recognize gain on all unrealized gains resulting from such sale to the extent they exceed \$627,000 (for 2010, adjusted annually; 2011 amount is \$636,000). A detailed discussion of the expatriation rules is outside the scope of this publication. We have prepared a separate publication that explains the expatriation rules in detail; please see the brochure entitled “Expatriation From the United States After June 17, 2008” for more information.

## II. Estate tax

### **Will I be considered a U.S. domiciliary for estate tax purposes?**

A person is considered to be domiciled in the United States for estate and gift tax purposes if they live in the United States with no present intention of leaving the United States.

A facts and circumstances test is used to determine domicile and takes into consideration the following factors:

- Statements of intent (in visa applications, tax returns, wills, etc.)
- Length of U.S. residence
- Whether the person has a green card
- Style of living in United States and abroad
- Ties to former country
- Country of citizenship
- Location of business interests
- Place where club and church affiliations, voting registration, and driver licenses are maintained

A person is considered a non-U.S. domiciliary (i.e. a nonresident alien) for estate and gift tax purposes if he or she is not considered a domiciliary under the facts and circumstances test described above.

Please be aware that residency for estate and gift tax purposes is determined differently than residency for income tax purposes. Thus, you may be a resident alien for income tax purposes, but a nonresident alien (hereinafter, non-U.S. domiciliary) for estate and gift tax purposes.

Also, please note that due to the subjective nature of this test, it is often difficult to determine an individual's domicile for U.S. estate and gift tax purposes with any degree of certainty. It is, therefore, important to consult with a professional experienced in international estate planning in order to determine your potential U.S. estate tax exposure and implement appropriate planning steps.

### **Which of my assets will be taxed in the United States upon my death?**

U.S. domiciliaries are taxed on the value of their worldwide assets owned at death in the same manner as U.S. citizens.

Non-U.S. domiciliaries are taxed only on the value of their U.S. "situs" assets. Generally, U.S. situs assets include real and tangible personal property located in the United States and stock of U.S. corporations. Please note that the definition of U.S. situs assets may be modified by an applicable Estate and Gift Tax Treaty.

## **Are there any credits or deductions available?**

Applicable exemption amounts are available against gift tax and estate tax for **U.S. citizens and domiciliaries**. In 2010, the lifetime cumulative exemption amount for gift tax purposes was \$1,000,000 of assets, and for estates of U.S. citizens and domiciliaries that do not elect carry-over basis, the estate tax exemption amount was \$5,000,000. However, any part of the \$1,000,000 used during life offset the \$5,000,000 available at death. In 2011 and 2012, U.S. citizens and domiciliaries may transfer \$5,000,000 (this amount will be indexed for inflation in 2012) free of either U.S. gift tax or U.S. estate tax. Any lifetime usage of the \$5,000,000 exemption will offset the \$5,000,000 available at death.

Upon the date of death (for persons dying in 2011–2012 and for persons dying in 2010 where the executor does not elect out of estate tax and into the carryover basis rules), the decedent's estate will receive a "step-up" in basis such that the estate's (and beneficiaries') basis in the decedent's assets will be the fair market value on the date of death.

If Congress does not act to continue or modify the estate tax rules as they are currently written, the estate and gift tax will continue in 2013 with a unified credit that exempts \$1,000,000 of assets from either U.S. estate or gift tax and a maximum tax rate of 55%.

**Non-U.S. citizens who are non-U.S. domiciliaries** are generally allowed a reduced estate tax exemption amount, which permits only \$60,000 of U.S. situs assets to be transferred free of U.S. estate tax. Note that this amount may be increased by an applicable Estate and Gift Tax Treaty. The election available to estates of decedents dying in 2010 to be exempt from estate tax is also available to non-U.S. domiciliaries, with a carry-over basis in the decedent's assets. The estates of non-U.S. citizen/non-U.S. domiciled decedents electing carryover basis receive a basis step-up of \$60,000 versus the \$1,300,000 available to the estates of U.S. citizens and U.S. domiciled persons. The additional \$3,000,000 basis step-up for transfers to a surviving spouse is available regardless of the status of the decedent as a U.S. citizen, U.S. domiciliary, or non-U.S. domiciliary.

## **How is jointly owned property taxed?**

Generally, the portion of jointly owned property that is taxed in the estate of a non-U.S. citizen is based upon who provided the "consideration" to purchase the property (i.e., whose assets were used to purchase the property) if the surviving spouse is not a U.S. citizen.

The portion of the property included in a decedent's estate is calculated based on the portion of consideration, which the decedent furnished for the property. Special rules apply to community property or property purchased with community funds.

If the surviving spouse is a U.S. citizen, generally, half of the value of jointly owned property will be included in the estate of the first spouse to die.

## **What are the tax rates?**

Estate and gift tax rates currently range from 18% to 35%. The rates are the same whether you are a U.S. citizen, U.S. domiciliary, or non-U.S. domiciliary.

Note that the particular U.S. state in which a non-U.S. citizen resides may impose additional estate and gift taxes.

## **Is double taxation a possibility?**

Yes. Since every country applies different standards to determine domicile, it is possible that two or more countries will consider the same person a domiciliary. Also, property may be taxable in the jurisdiction in which it is located or based on the residency of the recipient. In such cases, certain assets may be subject to estate tax in both countries. Proper planning along with Treaties and Foreign Tax Credits may eliminate or reduce double taxation.

## **Will property transferred to my spouse be subject to U.S. estate tax?**

The answer depends on whether your spouse is a U.S. citizen.

If your surviving spouse is a U.S. citizen, there is an unlimited marital deduction. In other words, an unlimited amount of assets can pass to your spouse without being subject to U.S. estate tax. Furthermore, if you and your spouse are U.S. citizens or domiciliaries and the executor of the estate of the first spouse to die makes an election on a timely filed estate tax return, any of the \$5,000,000 exemption (assuming a death in 2010 or 2011) that the first estate does not utilize will be available for the surviving spouse to use, in addition to his or her own \$5,000,000 exemption (referred to as “portability” of the exemption). If either you or your surviving spouse is not domiciled in the United States for estate tax purposes, portability is not available. If that is the case, the surviving spouse is only entitled to his or her own exemption based on his or her status as a U.S. citizen, U.S. domiciliary, or U.S. nondomiciliary at the time of his or her death and the exemption available under the U.S. estate tax rules in place at that time.

In addition, if your surviving spouse is not a U.S. citizen, the marital deduction is generally not allowed. However, a deferral of tax for assets passing to a non-U.S. citizen surviving spouse may be obtained if U.S. property passes through a Qualified Domestic Trust (QDOT). In addition, some Estate and Gift Tax Treaties allow for some form of a marital deduction in cases where such a deduction would not normally be available.

## **With which countries does the United States have Estate and Gift Tax Treaties?**

The U.S. currently has Estate and Gift Tax Treaties with the following 16 countries: Australia, Austria, Canada (through the income tax treaty), Denmark, Germany, Finland, France, Greece, Ireland, Italy, Japan, Netherlands, Norway, South Africa, Switzerland, and the United Kingdom.

## **III. Gift tax**

### **What transfers are subject to gift tax?**

U.S. gift tax is imposed on “taxable gifts” (total gifts less exclusions and deductions) made by U.S. citizens, U.S. domiciliaries, and non-U.S. domiciliaries as follows:

- U.S. citizens and domiciliaries are subject to gift tax on all transfers of property, regardless of where the property is located.
- Non-U.S. domiciliaries are subject to U.S. gift tax only on transfers of tangible personal property situated in the United States and real property situated in the United States. Gifts of intangible property, regardless of where located (such as stocks and bonds), made by a non-U.S. domiciliary are not subject to U.S. gift tax.

### **Are any transfers excluded from gift tax?**

There is an annual exclusion available which exempts up to \$13,000 per donee per year of “present interest” gifts from U.S. gift tax. U.S. citizens and domiciliaries can “gift split,” which, in effect, allows a married donor to exclude up to \$26,000 per donee per year. However, if either spouse is a non-U.S. domiciliary, gift splitting is not permitted.

The \$13,000 annual exclusion amount is increased for gifts to a non-U.S. citizen spouse to \$134,000 per year in 2010 (\$136,000 in 2011; indexed each year). In contrast, an unlimited amount can be gifted to a spouse who is a U.S. citizen pursuant to the unlimited marital deduction. It is important to note that a QDOT may not be used in order to obtain a marital deduction for transfers made to a non-U.S. citizen spouse during life. Also, an applicable Estate and Gift Tax Treaty may allow for some form of a marital deduction in cases where such a deduction would not normally be available.

### **Are any credits available?**

As mentioned above, in 2010, the cumulative lifetime gift tax exemption equivalent for U.S. citizens and domiciliaries was \$1,000,000. In 2011–2012, the gift tax exemption equivalent is \$5,000,000. However, any part of the \$1,000,000 or \$5,000,000 (depending on the year) used during life will offset the applicable exemption amount (\$5,000,000 in 2010, 2011, and 2012) available at death.

For non-U.S. domiciliaries, a \$60,000 applicable exemption amount is available for transfers made at death only. Other than the annual exclusion, there is no exemption amount available for lifetime transfers by non-U.S. domiciliaries.

## **IV. Generation-Skipping Transfer Taxes**

### **What transfers are subject to the Generation-Skipping Transfer Tax?**

The Generation-Skipping Transfer Tax (“GST tax”) is imposed on U.S. taxable gifts and bequests (i.e., transfers of worldwide assets by U.S. citizens and domiciliaries, gifts of U.S. situs tangible property by non-U.S. domiciliaries, and bequests of U.S. situs tangible and intangible property by non-U.S. domiciliaries) made to or for the benefit of persons who are two or more generations below that of the donor (e.g., a grandchild). GST tax is also imposed on gifts made to donees who are not related to the donor and who are more than 37.5 years younger than the donor.

### **Are any transfers excluded from GST tax?**

For GST transfers in 2011 and 2012, a GST exemption which exempts \$5,000,000 (indexed for inflation in 2012) of assets from GST tax is available for all transfers made both during life and after death by U.S. citizens, U.S. domiciliaries, and non-U.S. domiciliaries who are subject to GST tax. For GST transfers in 2010, the GST tax rate was zero, although special elections need to be considered in the case of 2010 transfers in trust for the benefit of skip persons. In 2011 and 2012, the highest GST tax rate is 35%.

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Deloitte Tax LLP has a team of professionals who specialize in estate planning for non-U.S. citizens. Additional information can be obtained by contacting Robert L. Dumont, Thomas P. Jaffa, or Karen Brodsky in our New York office at +1 212 436 2000.

Legal issues, such as wills or guardianship, have not been covered in the body of this text; an attorney should be consulted for assistance with such matters. The rules regarding the estate and gift taxation of non-U.S. citizens are extremely complex. This publication discusses only general concepts. It is not intended to answer all questions, only to serve as an introduction to the many issues which should be considered by non-U.S. citizens who live, work, or own property in the United States. An estate planning professional should be consulted to evaluate the consequences of each individual situation. This article does not constitute tax, legal, or other advice from Deloitte, which assumes no responsibility with respect to assessing or advising the reader as to tax, legal, or other consequences arising from the reader's particular situation.

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