Fundamentals of International Estate Planning

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The world is getting smaller and the laws pertaining to those subject to U.S. gift and estate tax (transfer tax) are becoming increasingly more complex. The U.S. estate tax applies not only to U.S. citizens, and U.S. citizens living abroad (known as expatriates) but also to U.S. permanent residents and non-resident aliens with U.S. situs assets. Residency is determined by a person's domicile or presence with the intent to remain indefinitely in the U.S. For transfer tax purposes, a noncitizen is a U.S. resident if he or she lives in the U.S. and intends to remain indefinitely.


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If, however, a person's intent is to return to his or her native country, that person is considered a non-resident alien (NRA) under the U.S. transfer tax law. A short review of the current U.S. estate tax regime may be helpful to understand the transfer tax consequences that apply to U.S. citizens, permanent residents and non-resident aliens.

All U.S. citizens and U.S. residents are subject to U.S. estate tax on their worldwide assets, with the first $11.2 million exempted from estate tax (the exemption amount is slated to sunset in 2026 and decrease to the pre-2018 exemption amount of $5.4 million). An unlimited amount may also be left to a surviving spouse if that spouse is a U.S. citizen, but if that spouse is not a U.S. citizen, the assets must given to a qualified domestic trust (QDOT) for that spouse's benefit to qualify for the unlimited marital deduction. In contrast, non-resident aliens are subject to U.S. estate tax only on their U.S. "situs" assets, with only the first $60,000 exempted from estate tax. Generally, U.S. situs assets include real estate located in the U.S., tangible personal property located in the U.S., shares of stock in U.S. corporations, and cash held with U.S. brokers.

There are two forms of international estate planning: inbound and outbound. Inbound planning is when a non-U.S. person invests in U.S. assets or contemplates a move to the U.S. Outbound planning pertains to a U.S. person that invests abroad. At death, a non-resident can transfer only $60,000 worth of U.S. situs property without paying U.S. estate tax and the top U.S. estate tax rate is 40 percent. As mentioned earlier, a non-resident is not entitled to an unlimited marital deduction, so transfers to a non-resident spouse are also subject to the $60,000 limit, unless the assets are placed in a qualified domestic trust (QDOT).

It is very common today for non U.S. persons to purchase real property in the U.S. for themselves or other family members. If U.S. real property is purchased in the name of the non-resident the property will potentially be subject to both U.S. gift and estate tax, barring a gift tax treaty with his native country. The current gift tax annual exclusion amount is $14,000 and therefore if a non-resident purchases a home for his or her child living in the U.S., the gift of real property could be subject to gift tax if it exceeds $14,000. A non U.S. resident might avoid the imposition of U.S. gift and estate tax by establishing a trust, in either the U.S. or a foreign country. Each has its benefits and disadvantages. U.S. law treats a foreign trust as a nonresident alien individual who is not present in the U.S. The gross income of a foreign trust that includes U.S. source income earned inside the foreign trust is not subject to U.S. tax. A foreign trust may be the preferred planning vehicle to hold real property or income producing U.S. assets when the beneficiaries are not U.S. citizens or residents. Another consideration may be purchasing U.S. real property in the name of a corporation if the nonresident does not plan on selling the property, as a sale may impose double taxation. It is vitally important for non U.S. persons to consult their accountants and attorneys prior to relocating to the U.S. to reduce overall taxation on their worldwide property.

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it is not uncommon to realize that you may wish to find a different way to satisfy the objectives outlined earlier. A PF may terminate its status under Internal Revenue Code section 507(b) by distributing all its net assets to one or more organizations holding a Determination Letter as described under IRC Section 509(a)(1). There is no termination tax required for this method of termination.

The successor public charity must have been in existence for a continuous period of more than 60 months before the transfer. The private foundation should file its Notice of Termination and final Form 990PF with the IRS subsequent to the terminating distribution. It is important to file the Notice after the distribution of assets, so the private foundation can report net assets equal to zero and limit the termination tax to zero.

Two examples of public charities qualified to receive the assets of the private foundation are Community Foundations and/or Donor Advised Funds.

Community foundations

Community foundations provide a well-established record of stewardship for philanthropy and a knowledge of the local community's needs. Fiduciary responsibility shifts from the board of directors of the private foundation to the board of the Community Foundation, and all administrative responsibility transfers to the Community Foundation's staff. The family terminating the private foundation can, if they desire, advise the Community Foundation by identifying areas of interest for grant making, which could continue the private foundation's original intent. We are fortunate here in South Florida to have several Community Foundations that will accommodate this such as the Jacobson Jewish Community Foundation, the South Palm Beach County Foundation and the Community Foundation for Palm Beach and Martin Counties, to name a few.

Donor-advised funds

Donor-advised funds offer a very low-cost mechanism for benefactors who wish to remain in the philanthropy business, but at a lower price point. After conversion to the donor-advised fund, the benefactors may continue to provide input about how the funds should be disbursed to charities.

Although the public charity sponsoring the donor-advised fund has final say over how the funds are invested and disbursed, they will usually follow the wishes of the family.

Benefits of a donor-advised fund are:

- Lower costs (usually 1 percent or less of the fund balance) and lower administrative burden.
- Benefactors have fewer responsibilities, record-keeping is simplified, and the sponsor assumes all back-office duties, such as compliance, state and federal filings, verifying grantee's tax exempt status and ensuring grant disbursements in accordance with IRS guidelines.
- There is no federal excise tax on net investment income.
- There is no minimum 5 percent payout of grants.

The steps to terminate the private foundation should include:

a) The Board adopts a Plan of Dissolution.

b) The state agency with jurisdiction over charities approves the Plan
(usually the Attorney General's Charities Bureau or a local Court).

c) Transmission of assets to successor entity, e.g. Community Foundation or Donor Advised Fund.

d) Prepare and file the Notice of Termination and final Form 990PF with the IRS.

e) Dissolve the private foundation's corporate status with Secretary of State.

f) Obtain tax clearance letter from state tax authority (if necessary).

g) Get ready to enjoy life with less bother from accountants and attorneys.

Private foundations still have their place in the world of charitable giving, but there are many in existence today that have outlived their utility and should be terminated for structures that are less burdensome, while still accomplishing the original intent of doing some good in the world.

Bibliography: American Endowment Foundation, "Terminating a Private Foundation" McAllister, Brian and Timothy Yoder, "Closing Up Shop: How to Successfully Shut Down a Private Foundation", Journal of Accountancy, July 2010. The New York Community Trust, "Terminating a Private Foundation", Professional Notes, Winter 2015. US Treasury, IRS Publication 4779, "Facts about Terminating or Merging Your Exempt Organization" 2009.

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As the world gets smaller, it is becoming more and more common for U.S. citizens to own property outside the U.S., work abroad, marry non U.S. citizens and have children. This adds complexities to transfer tax planning for the typical global family. It is important to understand the laws of the country of domicile that govern the distribution of wealth, and the treaties that may exist to minimize overall taxes for U.S. citizens, U.S. permanent residents, and non-residents.

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