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An Overview of Planning and Issue-Spotting for Multinational Individuals and Families

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Topics to be Covered

- What is meant by multinational for purposes of this presentation
- Common reasons multinational clients need estate planning
- The importance clarifying scope of engagement and detailed information gathering when working with multinational clients
- Transfer tax considerations and treaties
- Issues arising from having assets in multiple countries
- Gifting- U.S. person to non-U.S. person and receipt of gifts from non-U.S. person by U.S. person
- Pre-planning that can be done prior to moving to the U.S.
- Estate Planning for non-citizens or people with multiple citizenships and for citizens with significant foreign assets
- Probate issues that can arise with foreign assets

Multinational Clients

- In an increasingly global society it is common to have clients who are multinational in citizenship, residence, family, and/or location of assets and need special considerations taken while planning.
- In urban areas, such as Boston, with large academic and technology populations, having clients who are multinational is becoming the new normal.

Common Reasons For Multinational Client Planning

- Client is in the U.S., permanently or temporarily, and wants to put an estate plan in place.
- Client has a non-citizen spouse.
- Client is a non-U.S. resident who is planning on moving to the U.S. and wants to do pre-move planning.
- Client will receive a gift or inheritance from a non-U.S. person.
- Client is planning on giving up U.S. citizenship or green card and has to do pre-expatriation planning.
- Client is a non-U.S. person who holds or wishes to hold property in the U.S.
- Client is a U.S. person with significant foreign assets.

The Engagement Letter

- Make clear in the engagement letter that you are advising only on U.S. law and U.S. estate & gift (transfer) tax issues.
- If relevant, make clear to the client that any plan should be reviewed by legal counsel from the other jurisdiction or jurisdictions to ensure that there will be no unintended consequences in that jurisdiction to any plan you recommend.

First Conference and Information Gathering

- What are the client's goals for the planning?
- Which citizenships are involved for the client?
- Does the client have U.S. citizenship, a green card, or a U.S. visa?
- Is the client married and what is the citizenship (citizenships) of the spouse?

First Conference and Information Gathering - Continued

- Are there children, if so, where are the children located and what citizenships are involved?
- What foreign jurisdictions are involved?
- What types of foreign assets are involved?
  - Does the client have passive foreign investment company (PFIC) holdings?
- Is the client anticipating additional foreign assets in the form of a gift or inheritance?
- Is the client up to date on all foreign asset reporting requirements for the U.S.?
- Who are the client's intended beneficiaries and where is each one located?

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Transfer Tax Considerations

Is there a treaty in place between the U.S. and the other jurisdiction at issue that addresses gift and/or estate tax issues?

Transfer Tax Considerations

The U.S. has transfer tax treaties with:

Australia (estate and gift tax)

Austria (estate, gift, and GST tax)

Canada (income and estate tax treaty (and protocol)

Denmark (estate, gift, and GST tax)

Finland (estate tax)

France (estate, gift, and GST tax)

Germany (estate, gift, and GST tax)

Greece (estate tax)

Ireland (estate tax)

Italy (estate tax)

Japan (estate and gift tax)

The Netherlands (estate tax)

South Africa (estate tax)

Switzerland (estate tax)

The United Kingdom (estate and gift tax)

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Transfer Tax Considerations

- If there is a treaty, based on the client's circumstances, which jurisdiction will be the primary taxing authority?
  - Note that only the U.S. and the country of Eritrea impose a tax based on citizenship.
- In lieu of a treaty, will the client's transfer be subject to taxes in both jurisdictions?

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Pre-Move Planning for Non-U.S. Persons

Important to know whether this will be a permanent move to the U.S. or if this will only be for a short duration of time, such as to attend school or for a temporary work assignment. The needs and goals for the client may be very different depending on the duration of the anticipated residency in the U.S.

Pre-Move Planning for Non-U.S. Persons – Continue

- In the unlikely event that a client contacts you more than 5 years before their move, one planning technique that can be very useful is to recommend that the client establish a grantor type trust for the benefit of the client. The assets inside the trust will be able to grow tax free even after the client has become a U.S. person.
- Other options that do not require such a long timeline:
  - Work with the client to divest themselves of problematic assets prior to their move to the U.S. (for example PFICs).
  - Discuss with clients about making planned gifts prior to moving to the U.S. to avoid the imposition of U.S. gift tax.

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Real Estate Purchased by Non-U.S. Person

It is common for a Non-U.S. person to purchase real estate in the U.S. but have no intention of ever becoming a U.S. person. Common reasons are:

- Vacation home
- residence for child who is attending university in the U.S.

There are multiple options and related issues that need to be reviewed with your client before they move ahead with a purchase of U.S. real estate to avoid unintended consequences. (See examples on following slides)

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Real Estate Purchased by Non-U.S. Person - Continued

How will the real estate be held?

- Directly in the name of the non-U.S. client?
  - Easy option but will cause the client to be subject to U.S. estate taxes for the U.S. real estate if the client dies while owning it. Will also have to pass through probate.
  - Direct ownership will also not provide any form of creditor protection for the client, which may be an issue depending upon circumstances.
  - Will be subject to a 15% withholding at the time of sale under the foreign investment in real property act (FIRPTA)

Real Estate Purchased by Non-U.S. Person - Continued

How will the real estate be held? -continued

- In the name of the child or other relative of the client who will be residing in the property:
  - Will be a gift and may be subject to gift taxes and reporting requirements.
  - Will be includable in that person's estate for U.S. estate tax purposes.
  - Will be reachable by that person's creditors
  - Will also be subject to FIRPTA withholding at disposition if the person is not a U.S. person

Real Estate Purchased by Non-U.S. Person - Continued

How will the real estate be held? – continued

- In an entity such as a limited partnership, a limited liability company, a domestic corporation, or a foreign corporation.
  - The benefits of having the property in an entity is that it can avoid probate.
  - Negative aspects are the cost of setting up the entity and the ongoing administration of such. Depending upon the value of the real property and the planned duration that it will be owned it may not be cost effective to set up a complex structure to hold the property in.
  - If a trust holds the real estate, the issues multiply.

Real Estate Purchased by Non-U.S. Person - Continued

How will the real estate be paid for?

- Does the client have sufficient liquidity to purchase the property outright? (Some lenders are reluctant to work with non-U.S. persons due to the added burden of reporting requirements)

Before the client moves forward, it is recommended that the client engage counsel who regularly works in real estate law with a focus on international issues who can shepherd the acquisition of the property and structuring of the relevant entity, if any.

Gifts From U.S. Person to Non-U.S. Person

- The transfer will be subject to U.S. gift tax and, if applicable, U.S. generation skipping transfer taxes.
- If the transfer is a taxable gift then it must be reported on a timely filed Form 709.
- The U.S. donor will be able to apply their federal lifetime exemption to the transfer.

Gifts, bequests or inheritances from a Non-U.S. person to a U.S. person

- A U.S. recipient of foreign gifts, bequests, and/or inheritances from an individual or estate totaling more than $100,000 during a taxable year must report the transfer(s) (IRC section 6039F) on Form 3520. Individual gifts of $5,000 or more must be detailed.
- Gifts that fall under IRC section 2503(e)(payments of qualified medical and tuition expenses) do not need to be reported.

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Gifts, bequests or inheritances from a Non-U.S. person to a U.S. person

- If the gift was of U.S. situs realty or U.S. situs tangible personal property, the transfer will also trigger a U.S. gift tax to the donor.

- Transfers of intangible personal property will not trigger a U.S. gift tax for a non-U.S. person – even if the property happens to have a nexus with the U.S. such as stock in a U.S. company. (Note that gift tax may be applied if the non-U.S. person was overly aggressive in converting realty or tangible property into intangible for the purpose of avoiding tax.)

Specific Issues Related to Foreign Trusts and U.S. Beneficiaries

What is a foreign trust for U.S. tax purposes?

- Since 1996 there has been a two-part test for determining whether or not a trust is a "foreign trust":
  - The U.S. Court Test – does the U.S. court exercise primary supervision over the administration of the trust? (IRC section 7701(a)(30)(E))
  - The Control Test – do one or more U.S. persons have authority to control, by vote or otherwise, all substantial decisions of the trust? (IRC section 7701(a)(30)(E))
- If a trust does not satisfy both parts then it is deemed a foreign trust.
- Potential traps – foreign protector, foreign powerholder

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Specific Issues Related to Foreign Trusts and U.S. Beneficiaries

- One major issue with foreign trusts is the imposition of "throwback tax" on U.S. beneficiaries.
  - Throwback tax (IRC 667 & 668) is a tax imposed upon all accumulated income in the trust, including gains.
  - This can occur when the trust has not been distributing out all income on an annual basis.
  - This tax can be incredibly punitive and encompass up to 100% of the distribution received by the beneficiary

Specific Issues Related to Foreign Trusts and U.S. Beneficiaries

Way to avoid throwback tax through proper trust structuring:

- If you are part of the original planning involving the trust, you may be able to avoid the throwback tax through structuring the trust to comply with IRC section 663.
  - Under the provisions of IRC section 663, if the trust provides that all distributions to the U.S. person are structured as no more than three (3) specific bequests of stated amounts then the throwback tax will not be imposed on such distributions since the distributions are not deemed distributions of income under section 662(a).
- If you are not involved with the trust at the initial planning stages this option may still be possible if the trustee has the power to establish and fund a new trust.

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Estate Planning for Multinational Clients

- **Are any of the assets held in jurisdictions with forced heirship laws?**
  - Does the client care and want the property to pass in a different manner? If so, local counsel for that jurisdiction should be consulted with to discuss possible options.
- **Whether or not separate Wills for each jurisdiction is appropriate?**
  - We recommend a separate Will where there are assets in a different country and the client has the ability to direct the disposition of such. Local counsel in that country should be coordinated to draft such documents.
  - Any documents put in place in the U.S. should specifically reference the foreign estate documents and you need to be careful to not inadvertently revoke any documents or include conflicting provisions.

Estate Planning for Multinational Clients

- When planning for a non-U.S. citizen the issue of marital deduction for state estate tax and federal estate tax purposes must be taken into account:
  - While the clients may not have to worry about federal estate taxes due to the high exemption amounts, the marital deduction can still be critical when planning in states where there is a state level estate tax.
  - Our practice is to include a springing Qualified Domestic Trust (QDOT) provision in the trusts to ensure that assets passing to the foreign spouse under the trust can qualify for the marital deduction if the spouse is not a U.S. citizen at the time of the client's death (or when the estate tax return is due)

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Questions?

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Note: The materials provided herein are necessarily brief, do not detail all planning aspects of the issues and are for educational and informational purposes only and should not be construed as legal advice.

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