

THE MULTINATIONAL COUPLE: PROBLEMS ASSOCIATED WITH NONCITIZEN SPOUSES

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I. Consideration of Marital Regimes

Family mobility presents challenging tax and estate planning considerations when one or more family members move to the United States or invest in U.S. property, as well as when Americans move abroad, invest in foreign property, or have non-U.S. citizen spouses or foreign beneficiaries. A multinational couple may be exposed to more than one marital regime for a variety of reasons, including where they were married, changes in domicile, marital property agreements and co-ownership of property. International tax and estate planning necessarily involves the consideration of foreign laws regarding marital rights and succession, as well as numerous conflict of laws problems. Foreign property and inheritance laws are often quite different from those of the United States.

Multinational estate planning often raises principals of law derived from civil and common law, as well as other regimes, such as Sharia law and that of the Hindu undivided family, among others, many of which are not second nature to U.S. estate and tax planning advisors. In order to do a proper estate plan for a multinational couple, one must ascertain which matrimonial property regime will apply with respect to their various assets in order to determine how assets will be treated during marriage and how they will be divided upon death or divorce. The applicable matrimonial regime will govern the ownership of assets owned by the spouses, the income and gains derived from the property, the management and disposition of those assets, and the resulting income and transfer tax consequences to a couple, as well as reporting requirements. For example, in some civil law jurisdictions spouses are deemed to own property in the community unless they have affirmatively elected a separate property regime. Determining property interests of a married couple in the international context will often turn on a conflict of laws analysis: 1) which country's conflict of laws rules should apply; and 2) which country's marital property rules should apply.

Many foreign jurisdictions provide for community property as their default marital regime. For couples married in those jurisdictions or those who elect into a community property regime, great care should be taken when changes to the marital regime are made, whether intentionally or unintentionally. If a couple changes from a separate to a community property regime, U.S. gift tax exposure may be triggered.

A. General Overview of Marital Property Rules in the United States

In the United States marital property rights of spouses during marriage establish the ownership, management and disposition of property, the income and gains that derive from the property, the income tax consequences attributable to the property, and rights of creditors with respect to the property. Further, these marital property rights determine the division of property upon separation or dissolution, as well as the succession rights to and the administration of property upon death, federal and state transfer and inheritance tax liabilities attributable to such property and related creditors claims.

Note that some U.S. states, including California, extend to registered domestic partners almost all of the rights, benefits and protections that apply to spouses under law, both during and upon termination of the union.¹

Each state within the United States has its own laws on marriage, marital property rights, inheritance and state taxation. In order to plan effectively for a couple, the applicable marital property regime first must be established so as to determine and define the marital property. As in the international context, in the event of a dispute the forum state will apply its own set of conflict of laws principles to determine the law applicable to marital property.

B. General Overview of U.S. Community and Common Law Property Regimes

Common law is the dominant marital property system in the United States under laws originating in the United Kingdom, while ten states have adopted the community property system of civil law origin. The community property states are Arizona, California, Idaho, Louisiana, Nevada, New Mexico, Texas, and Washington. Alaska and Wisconsin also recognize some form of community property. Puerto Rico, a U.S. territory, is also a community property jurisdiction. The theory under common law is that each spouse has separate legal and property rights with respect to his or her assets. In contrast, under community property law, generally each spouse owns a 50 percent interest in all property acquired during a valid marriage regardless of which spouse acquired the property.² In community property states, spouses may also hold separate property.

II. Conflict of Laws/Domicile Issues.

The case of *Charania v. Commissioner*³ illustrates the difficulties involved in ascertaining marital property rights of a couple's assets and how they may be taxed upon the death of a spouse. Noordin and Farhana Charania were born and married in Uganda and citizens of the United Kingdom. During their marriage, they were exiled from Uganda by its then dictator, Idi Amin, and fled to Belgium with no assets. At the time of their exile, Uganda was governed by British common law principles and Belgium was a community property jurisdiction. The Charanias acquired their assets while living in Belgium, where the couple lived for 30 years until Mr. Charania died. While in Belgium, Mr. Charania purchased stock in Citicorp which ultimately became Citigroup. At the time of his death, Mr. Charania owned 250,000 shares of Citigroup stock titled in his name alone, held by Fortis Bank, Hong Kong, and valued at almost \$12 million.

The IRS asserted that the entire value of the Citigroup shares were included in Mr. Charania's estate, while the estate contended that only one-half of the shares should be included on the grounds that the shares were the couple's community property under Belgian law. The decedent's will followed Belgian forced heirship law, leaving one third of his property to his wife and the balance equally to his two children. The estate argued unsuccessfully that the marital domicile was changed to Belgium so that community property principles applied to the stock ownership.

In *Charania*, the U.S. Tax Court undertook an analysis of whether marital domiciles were mutable or immutable under British common law. The Court found there was no evidence

presented that a Belgian Court would recognize mutability, even where the marital domicile had changed because of expulsion from the original marital domicile. The important fact to the Court was that the couple had taken no steps to change the marital law applicable to their property as allowed under Belgian law. Accordingly, the Court concluded that there was no basis for mutation and the Charanias were not governed by Belgian community property law since they had done nothing to cause themselves to be governed by that law. As such, the Court ruled that Mr. Charania's entire holding of Citigroup stock was subject to U.S. estate tax.

The Charania case demonstrates certain issues that may arise in dealing with international taxpayers and their assets, particularly with respect to marital property regimes. This case applies U.S. law and a court of a foreign jurisdiction could easily make a different determination under its own laws. Perhaps the most important lesson from the case is that solid tax advice could have saved the estate from U.S. estate tax on any of the stock held by Mr. Charania – with proper structuring of the stock holdings by interposing a foreign corporation, the property interest owned at date of death could have been treated as foreign situs property not subject to U.S. estate tax.

III. U.S. Tax Issues Arising During Marriage

A. U.S. Income Tax Considerations

a. Will the Non-Citizen Spouse be Considered a U.S. Tax Resident for Income Tax Purposes?

While a U.S. citizen is subject to U.S. income taxation on his or her worldwide income⁴, regardless of residency, the income tax treatment to his or her spouse will depend upon the non-citizen spouse's residency for U.S. income tax purposes. An individual who is not a U.S. citizen is treated as a U.S. tax resident during a particular taxable year, and, thus, is subject to U.S. federal income tax on a worldwide basis (unless an applicable treaty provides otherwise), if such individual either is a "lawful permanent resident" of the United States under United States immigration laws *at any time* during such calendar year (*i.e.*, holds a green card), or satisfies the "substantial presence test" described below. It is also possible to elect to be treated as a U.S. resident for this purpose (the "first-year election").⁵

i. The Substantial Presence Test

Under the substantial presence test, an individual who is not a U.S. citizen or a "green card" holder will be treated as a U.S. tax resident during a particular calendar year if he or she is physically present in the United States for at least 31 days during that calendar year *and*, under the two-year look back rule discussed below, is considered to be present for 183 days or more during such period (the "Substantial Presence Test").⁶ The Substantial Presence Test therefore considers not only time spent in the U.S. during the year being tested, but also the two years prior to such year.

An individual will be treated as a U.S. resident under the two-year look-back rule if the sum of (i) the number of days of his or her physical presence in the United States in the current calendar year, (ii) one-third (1/3) the number of days of his or her physical presence in the United

States in the first preceding calendar year, and (iii) one-sixth (1/6) the number of days of his or her physical presence in the United States in the second preceding calendar year, equals or exceeds 183 days.⁷

For example, assume that a French individual comes to the United States on September 1, 2016 and continuously stays in the United States for the remainder of 2016. Assume further that this person was present in the United States for 150 days in 2015 and 180 days in 2014. For purposes of determining the individual's status under the substantial presence test for 2016, each day such individual spends in the United States in 2016 will count as one day (totaling 122 days in 2016), each day spent in the United States in 2015 will count as one third of a day (totaling 50 "weighted" days in 2015), and each day spent in 2014 will count as one sixth of a day (totaling 30 "weighted" days in 2014). The total number of "weighted" days for 2016 will therefore be 202 (*i.e.*, 122 + 50 + 30), and because 202 days exceeds 183 days, the individual satisfies the substantial presence test for the taxable year 2016 and may be taxed as a U.S. tax resident for that year.

An alien is considered to be present in the United States on any day that he or she is physically present in the United States at any time during the day.⁸ Therefore, partial days, including the day of arrival and day of departure, count as a day of presence in the United States.⁹ In addition, certain individuals are "exempt" and their days of presence in the United States are not counted for purposes of the Substantial Presence Test. These exempt individuals include, among others, certain teachers, students, professional athletes competing in charitable sports events, and foreign government related persons.¹⁰ Exceptions also apply for certain medical emergencies.¹¹

Exception to Residency Status Under the Substantial Presence Test—Closer Connection Exception. An exception to residency status may be available to an individual who is not a U.S. citizen or green card holder but who meets the Substantial Presence Test if the individual meets a "closer connection" test. Under this test, the individual who has not taken steps to become a permanent resident must meet **all** three of the following conditions to avoid residency status:

- (i) he or she is present in the United States for less than 183 days during the current year;
- (ii) he or she has maintained a "tax home" in a foreign country during the current year; and
- (iii) he or she has a "closer connection" to the foreign country in which his or her tax home is located than to the United States.¹²

For purposes of the closer connection exception, a tax home is a person's regular or principal place of business.¹³ If he or she has no regular or principal place of business, then his or her tax home is his or her regular place of abode in a real and substantial sense. If he or she has neither, his or her tax home is the country where he or she works.¹⁴ This tax home must be in existence for the entire current year, and must be located in the same foreign country where the closer connection is claimed.¹⁵

The factors considered in determining whether a person has a closer connection include the location of the person's permanent home, family and personal belongings, the location of cultural and religious organizations to which he or she belongs, the location of routine banking activities, the location where he or she conducts business activities, the jurisdiction that issued his or her driver's license, where he or she votes, the country he or she designates as his or her residence on forms and documents and the types of forms and documents he or she files, including tax forms.¹⁶ The closer connection exception will not apply with respect to any current year if the taxpayer had an application for adjustment of status pending, or such individual took other steps to apply for status as a lawful permanent resident of the United States.¹⁷ In order to claim the closer connection exception, the foreign person must timely file a statement with the IRS (Form 8840 is used for this purpose).¹⁸

Importantly, although not covered here, there are special rules applicable to residency starting and termination dates, as well as to dual residency where relief may be obtained under an income tax treaty to avoid U.S. income tax taxation.

ii. U.S. Income Taxation of Nonresident Aliens.

1. In General

Whereas U.S. citizens and resident aliens are subject to U.S. income tax on their worldwide income, nonresident aliens ("NRAs") are subject to U.S. income tax only on certain items of U.S. source income.¹⁹ NRAs are subject to a 30% tax (or such lesser rate as is determined by an applicable income tax treaty) on most items of U.S. source fixed or determinable, annual or periodical ("FDAP") income that are not effectively connected with the conduct of a trade or business in the U.S.²⁰ FDAP income includes certain dividends, interest, rents, compensation, annuities and royalties.²¹

The 30% tax liability is generally collected by withholding at source, subject to reduction by an applicable income tax treaty.²² Some income items are specifically excluded from FDAP withholding, including OID, portfolio interest and interest on deposits with U.S. banks (that is not effectively connected with a U.S. trade or business). Portfolio interest includes most U.S. source interest paid to a foreign lender on an obligation that is in registered form.²³ Such interest generally is exempt from tax provided that the foreign lender owns less than 10% of the entity paying the interest.²⁴

NRAs are subject to 30% tax on certain timber, iron and ore gains²⁵ and gains from the sale of certain intangible property (patents, copyrights, goodwill, trademarks, franchises, etc.) to the extent such gains are payments that are contingent on the productivity, use, or disposition of the property or interest sold or exchanged.²⁶ U.S. source capital gains are subject to the 30% flat tax only if an NRA is present in the U.S. for at least 183 days during the calendar year.²⁷ Special rules apply to the disposition of real estate, discussed below.

Generally, no withholding is required for any income that is effectively connected with the conduct of a U.S. trade or business ("ECI") (other than compensation for personal services).²⁸

Instead NRAs file U.S. income tax returns and are taxed on a net basis on ECI at normal graduated rates.²⁹ Whether income is “effectively connected” is a critical inquiry in this analysis. Generally, foreign source income is not ECI, with certain exceptions for rents, royalties, dividends and interest attributable to a U.S. office. U.S. real estate gains are treated as ECI whether or not an NRA is engaged in a U.S. business. In order to avoid withholding, persons conducting U.S. trades or businesses are required to file certain prescribed forms with withholding agents for each tax year for which such persons will be entitled to the income, and before payment of the income in respect of which it applies.

An NRA may elect to treat income from U.S. real property which is not “effectively connected” (e.g., property subject to a triple-net lease) as if it were so for tax purposes so as to avoid the 30% flat tax.³⁰ This election, once made, applies for all subsequent years, unless revoked with IRS consent. This election can be advantageous because it allows deductions associated with the property to be claimed.

All persons having the control, receipt, custody, disposal, or payment of U.S.-source FDAP income of any NRA or foreign partnership (“Withholding Agents”) must deduct and withhold a 30% tax (or lesser rate imposed by an applicable income tax treaty).³¹ If the Withholding Agent does not withhold and the foreign person does not satisfy its withholding tax obligation, the Withholding Agent and the foreign person are liable for the tax and any interest and penalties.³²

Every Withholding Agent is generally required to file Forms 1042 and 1042S on or before March 15 reporting the tax required to be withheld during the preceding calendar year.³³ Even if no tax was withheld by the Withholding Agent, Form 1042 is nevertheless required to be filed if the Withholding Agent was required to prepare a Form 1042S with respect to any payments made during the year.³⁴ A copy of the Form 1042S must be provided by the Withholding Agent to the recipient.³⁵

The entire amount of income from which tax is required to be withheld must be included in gross income on the income recipient’s return, without deduction for the withheld amount, but the tax withheld is allowed as a credit against the total income tax computed on the taxpayer’s return.³⁶

The method for securing the reduced withholding rate as may be provided by an applicable income tax treaty is prescribed by Regulations.³⁷ The NRA generally claims entitlement to treaty benefits by providing Form W-8BEN to the Withholding Agent.³⁸ To claim exemption from withholding on payments for personal services, Form 8233 is used instead of Form W-8BEN.³⁹

An NRA’s distributable share of a U.S. (“domestic”) partnership’s FDAP income is subject to the 30% withholding by the partnership.⁴⁰ The 30% withholding may also apply to the portion of the NRA’s distribution of income from a trust or estate that is attributable to the trust’s or estate’s FDAP income. The foreign partnership, pass-through entity, agent or other intermediary provides the Withholding Agent with Form W-8IMY.⁴¹

In determining an NRA’s taxable income, only deductions related to Effectively Connected Income may be claimed.⁴² In addition, an NRA is allowed to deduct (i) certain casualty

or theft losses (if the loss is of property located within the United States); (ii) charitable contributions; and (iii) personal exemptions.⁴³

In computing the tax on his or her ECI, an NRA is not entitled to the standard deduction,⁴⁴ cannot qualify as a head of household,⁴⁵ and must generally compute his or her tax based on the rate schedules for single individuals or married individuals filing separately.⁴⁶ The alternative minimum tax may also apply to an NRA depending on his or her individual circumstances.⁴⁷

To obtain the benefit of deductions, an NRA must file a true and accurate U.S. Federal income tax return.⁴⁸ Under the Regulations, the return must be filed within 16 months of the prescribed date in order to preserve the right to claim deductions and credits.⁴⁹ In 2006, these Regulations were held to be invalid by the U.S. Tax Court in *Swallows Holdings, Ltd. v. Commissioner*.⁵⁰ However, the IRS won a major victory when the U.S. Third Circuit Court of Appeals overturned the Tax Court and upheld the validity of the Regulations.⁵¹ As a practical matter, the result in *Swallows* means that foreign corporations intending to claim deductions and credits in the Third Circuit must heed the timely filing requirement of the Regulations.⁵² The decision leaves many unanswered questions in its wake, particularly about judicial deference to the Regulations.

If an NRA conducts limited activities in the United States in a taxable year and determines that the activities do not give rise to gross ECI, the NRA may file a “protective” tax return to protect his or her claim to deductions and credits. He or she is not required to report any gross income on the return but must attach a statement to the return.⁵³

2. Treaty Income

An NRA who is a resident of a country with which the United States has concluded an income tax treaty may be able to reduce (or eliminate) the U.S. income tax on his or her ECI. For example, under both the U.S. and OECD Model Income Tax Treaties, simply engaging in a trade or business within the United States is not a sufficient basis for the imposition of U.S. income tax. Rather, an NRA will be subject to U.S. income tax under these treaties only if he or she carries on business through a “permanent establishment” situated in the United States.⁵⁴ A “permanent establishment” is defined as a “fixed place of business.”⁵⁵ Examples of a fixed place of business include a place of management, a branch, an office, a factory, a workshop, and a place where natural resources are extracted.⁵⁶

An NRA who relies on a U.S. tax treaty for an exemption from U.S. tax on ECI is required to file IRS Form 8833 to disclose such reliance.⁵⁷

3. U.S. Real Property Taxation

Under the Foreign Investment In Real Property Tax Act of 1980 (“FIRPTA”),⁵⁸ an NRA’s gains or losses from the disposition of both direct and certain indirect interests in U.S. real property are treated as gains or losses effectively connected with the conduct of a U.S. trade or business and, therefore, ECI.⁵⁹ A complete description of the FIRPTA provisions is beyond the scope of this article. Generally, the taxable U.S. real property interests include interests in

domestic corporations that are predominantly invested in U.S. real estate, as well as indirect ownership interests in U.S. real estate.⁶⁰ FIRPTA provides, in part, as follows:

(1) The term “disposition” specifically includes contributions to the capital of a foreign corporation.⁶¹

(2) The term “U.S. real property interest” (“USRPI”) is broadly defined and includes an interest (other than solely as a creditor) in a corporation which at any time during the previous five years (or the period owned, if less) was a “U.S. real property holding corporation” (“USRPHC”), defined as any U.S. corporation holding U.S. real property interests with a value equal to at least 50% of the sum of the corporation’s U.S. and foreign real property interests plus assets used in the trade or business.⁶²

(i) If, as of the date of the disposition, the corporation had no USRPIs, and had disposed of such interests entirely in taxable transactions, the corporation will not be treated as a USRPHC.⁶³

(ii) For this purpose, an interest in a publicly-traded class of stock will not constitute a USRPI if the NRA has held 5% or less of such class of stock throughout the five-year testing period.⁶⁴

(3) The FIRPTA tax is enforced by a withholding requirement imposed on the transferee of a USRPI.⁶⁵

(i) As a general rule, the transferee (buyer) must withhold 15% (this amount was increased in 2015 from 10%) of the amount realized on the disposition.⁶⁶ The amount withheld must be reported and paid to the IRS within 20 days by filing Forms 8288 and 8288-A.⁶⁷

(ii) The withholding obligation is not reduced or otherwise affected if the cash proceeds are less than the amount required to be withheld.⁶⁸ Further, if the transferee does not withhold and pay over the required amount, he or she may be personally liable for payment and any penalties and interest.⁶⁹

(iii) The withholding amount is subject to a ceiling equal to the transferor’s maximum tax liability.⁷⁰ To establish that the maximum tax liability is less than 15% of the amount realized, so as to reduce the withholding obligation, a withholding certificate should be obtained from the IRS.⁷¹

(iv) The NRA transferor is required to file a Form 1040NR reporting the gain as ECI and pay any balance of tax due.⁷²

(v) If the amount withheld exceeds the tax due, the transferor may seek a refund on his or her filed return, or may apply for an early refund.⁷³

4. Joint Returns

In the United States spouses may file a joint income tax return and they will be jointly and severally liable for the tax on all of the income reported, whether it is community or separate.⁷⁴ However, joint return may be filed if either spouse is a non-U.S. resident. Spouses may also file separate returns with each spouse being taxed on 50 percent of the total community property income and 100 percent of his or her separate property income. The community property states are not consistent in how income from separate property is characterized.⁷⁵ California and several other community property states follow the rule that income generated during marriage from separate property is separate property, except to the extent that the income is generated from community property skills and labor.⁷⁶ Other community property states follow the rule that all income from separate property is characterized as community property.⁷⁷ The IRS' ability to collect taxes owned by only one spouse from the couple's community assets is dependent upon state law.

B. U.S. Transfer Tax Considerations

a. Will the Spouse be Considered a U.S. Domiciliary for Transfer Tax Purposes?

Like the U.S. income tax, U.S. transfer taxes apply to U.S. citizens and U.S. residents on a worldwide basis. Unlike the mechanical test for determining U.S. income tax residency, however, residency for U.S. transfer tax purposes is much less straightforward. For U.S. transfer tax purposes, residency determination is based on the common law principles of **domicile**. If an alien is a resident for U.S. income tax purposes, he or she may not be treated as a resident for U.S. transfer tax purposes. Similarly, an alien who is treated as a U.S. domiciliary for transfer tax purposes may not be treated as a resident for U.S. income tax purposes.

For purposes of U.S. transfer taxes, an alien is considered a U.S. resident if he or she is domiciled in the United States at the time of the inter vivos or testamentary transfer event. Whether a person is a U.S. domiciliary depends on the person's intent.⁷⁸ If an alien physically moves to the United States, even for a brief period, and has no definite or present intention of leaving the United States, he or she will be a U.S. domiciliary for estate, gift and generation-skipping transfer ("GST") tax purposes.⁷⁹ A person may have only one domicile and must always have a domicile, and intention to change domicile will not be effective unless the change is accompanied by actual removal.

Along with a person's intent to make the United States his or her permanent home, the person must be present in the United States when he or she makes that decision and have the ability to make an informed and intelligent decision as to his or her domicile. The determination of intent for establishing domicile is one of facts and circumstances that may turn on many factors, none of which is determinative. The authority in this area is sparse and highly fact-specific. Some factors on which the IRS and courts have focused are: (i) the length of time spent in the United States and abroad and the amount of travel to and from the United States and between other countries; (ii) the value, size, and locations of the individual's homes and whether he or she owned or rented them; (iii) visas, work permits and similar immigration documents; (iv) whether the

individual spends time in a place due to poor health, for pleasure, to avoid political problems in another country, etc.; (v) the location of valuable or meaningful tangible personal property; (vi) the location of the individual's family and close friends; (vii) the location of the individual's religious and social affiliations or participation in civic affairs; (viii) the location of the individual's business interests; (ix) the places where the individual states that he or she resides in legal documents; (x) the jurisdiction where the individual is registered to vote; (xi) the jurisdiction that issued the individual's driver's license; and (xii) the individual's income tax filing status.⁸⁰

Immigration laws do not require that a green card holder intend to remain in the United States permanently. However, the U.S. Tax Court has held that an individual who acquires the immigration status of a "permanent resident of the United States" (i.e., acquires a green card, rather than a non-permanent visa) will be presumed to have acquired U.S. domicile for U.S. transfer tax purposes.⁸¹ In *Estate of Khan v. Commissioner*, the court found that a Pakistani citizen was a U.S. resident when he died even though he had lived in Pakistan for five years before his death.⁸² The Tax Court held that such U.S. domicile, once acquired, will continue even if the individual subsequently leaves the United States for an extended period (in *Khan*, five years) unless it can be shown that the individual never intended to return to the United States to reside.⁸³ Note that in *Khan*, the taxpayer took the position that the decedent was a U.S. resident so that the estate would be entitled to a larger estate tax credit. The issue has not arisen in published authority as to whether the position would be sustained against a taxpayer just as it was used in the decedent's favor in *Khan*.

Despite the importance of holding a green card expressed in *Khan*, there is other authority that indicates that immigration status is not necessarily conclusive of domicile. The IRS ruled that a foreign decedent who was an employee working in the United States for an international company on a G-4-Visa and who remained in the United States until his death was a U.S. domiciliary because he resided in the United States and had formed the intent to remain in the United States indefinitely.⁸⁴ The IRS also ruled that a decedent illegal alien had U.S. estate tax domicile status where he had the legal capacity to acquire domicile, he was physically present in the United States at the time of death and he had a current intention to make his home in the United States even though he was subject to deportation.⁸⁵

In *Estate of Jack v. U.S.*,⁸⁶ the Federal Claims Court considered the immigration documents of a decedent Canadian citizen who was employed in the United States at his death under a temporary visa. The court rejected the estate's argument that the formation of the requisite intent would be in violation of the terms of the visa, so as to preclude the IRS from attempting to show that the decedent had the intent to establish domicile. Although the case does not hold that the decedent was in fact domiciled in the United States, the fact that he was present in the United States on a temporary, non-immigrant visa did not preclude the IRS from proceeding to show that he was domiciled in the United States.⁸⁷

b. What Assets of Nonresident Aliens Are Subject to U.S. Transfer Taxes?

The estate of an NRA who is not domiciled in the United States is subject to estate taxes only on certain limited assets. Generally, NRAs are subject to U.S. estate tax only on U.S. situs

property, with no credit for foreign death taxes paid.⁸⁸ Gifts by an NRA of interests in U.S. real estate and tangible personal property located in the United States are subject to U.S. gift taxes, but not gifts of intangible property.⁸⁹

i. Federal Estate Tax Rules

U.S. situs property for federal estate tax purposes includes the following: (1) real property located in the United States;⁹⁰ (2) tangible personal property located in the United States, including cash;⁹¹ (3) certain debt obligations of a U.S. person or governmental agency and short term OID obligations;⁹² (4) shares of stock issued by a U.S. corporation (irrespective of the location of stock certificates);⁹³ and (5) certain partnerships that engage in U.S. trades or businesses or have property deemed to have a U.S. situs.⁹⁴

If U.S. real estate owned by a non-domiciled alien is subject to recourse debt, then the full fair market value of the real estate is reported on the federal estate tax return with a corresponding deduction for a portion of the debt. This portion is equal to a fraction, the numerator of which is equal to the value of the decedent's total U.S. situs property and the denominator of which is equal to the value of the decedent's worldwide estate. In order to obtain the deduction for a portion of the debt, however, the non-domiciled alien must disclose the value of the decedent's worldwide assets and debt.⁹⁵

With respect to real estate subject to nonrecourse debt, only the equity value of the property is included on the federal estate tax return and no disclosure of worldwide assets is required.⁹⁶ Foreign persons often encumber their U.S. real estate to minimize federal estate tax reporting of their worldwide assets.

Certain assets that one might think would have a U.S. situs do not, including demand deposits in U.S. banks and many debt instruments of U.S. issuers. The policy behind these exceptions is to encourage foreign investment in U.S. corporate and government debt instruments. The portfolio debt exception effectively exempts most publicly-traded debt securities of U.S. companies and most U.S. governmental obligations owned by non-domiciled aliens from federal estate tax. Debt obligations of non-U.S. persons are considered to be non-U.S. situs assets. Shares of stock in a foreign corporation are deemed to be situated outside of the United States and thus, not subject to U.S. estate tax.⁹⁷ Similarly, proceeds from an insurance policy on the life of a non-domiciled alien are considered to be situated outside of the United States, even if the policy is issued by a U.S. life insurance company.⁹⁸ If a non-domiciled alien owns a life insurance policy on the life of another person, and that policy is a U.S. situs asset, the value of the policy (as opposed to the proceeds) will be includable in the alien's U.S. estate.

The law is not clear on whether an interest in a partnership or limited liability company is included in the U.S. gross estate of a non-domiciled alien. Based on existing authority, there are several approaches to the determination of the situs of a partnership interest owned by an NRA: (1) situs based upon the holder's domicile; (2) situs based upon the partnership's assets; or (3) situs based upon the location of the trade or business of the partnership. If the law of the place of creation does not treat the partnership as a legal entity, or if the partnership dissolves upon the

death of a partner, then the non-domiciled alien's gross estate will include his or her pro rata share of the underlying partnership property which is deemed situated in the United States.⁹⁹

If the law of the place of creation treats the partnership as a legal entity which survives the death of a partner, then the partnership interest will be treated as the unit of ownership and the situs of such interest is not clear under current law. If the partnership interest is treated as intangible personal property, then the situs should depend upon the domicile of the decedent under *Blodget v. Silberman*.¹⁰⁰ The IRS, however, disagreed with the *Blodget* decision in Revenue Ruling 55-701,¹⁰¹ finding instead that the situs of a partnership interest was the location of the partnership's business, but citing *Blodget* with approval for the idea that the determination of situs does not depend on the location of the partnership's underlying assets.

Another case, however, supports the aggregate theory. In *Sanchez v. Bowers*, the Second Circuit ruled that the dissolution of a foreign entity upon the death of one of its owners caused the underlying assets to be included in the decedent's estate to the extent that they consisted of U.S. situs assets.¹⁰²

Treaties will often decide the issue, generally in favor of treating the partnership interest as an intangible asset taxable by the jurisdiction where the decedent was domiciled. If the partnership enterprise is at least 50% invested in real property, the interest may be taxed by the jurisdiction of the situs of the property.

Similarly, an NRA decedent's interest in a trust holding U.S. situs assets will be subject to estate tax to the extent the interest is of a type that would cause the trust to be includable in the estate of a U.S. citizen or resident, as discussed below.

A nonresident may be *deemed* to own property situated in the United States at death as a result of certain transfers of U.S. situs property during life. Property of a nonresident decedent will be deemed to be situated in the United States, and potentially taxable pursuant to this rule, if such property was transferred at a time when it was situated in the United States, and if the deceased transferor retained sufficient rights in or powers over the property after making the transfer.¹⁰³ Under this rule, regardless of where the property is situated at the time of the transferor's death, the property is included in the transferor's estate for U.S. tax purposes, at its then fair market value.¹⁰⁴ This deemed situs rule is often a trap for the unwary.

For U.S. estate tax purposes, a U.S. citizen may claim a credit for the amount of death taxes actually paid to any foreign country attributable to property situated in that country and included in the gross estate of the decedent.¹⁰⁵ It is important to check whether the credit may be affected by any estate or gift tax treaty between the United States and the foreign country imposing the tax.

ii. Gift Tax Rules

The definition of taxable U.S. situs gifts is more limited than that for property subject to estate tax. Only gifts of U.S. real property and tangible personal property situated in the United States are subject to gift tax if made by non-domiciled aliens.¹⁰⁶ Transfers of U.S. situs intangible

personal property are not subject to gift tax even if the intangible property has a U.S. situs, unless the donor is a non-domiciled alien who previously expatriated from the United States.¹⁰⁷

Gifts of currency that take place in the United States and gifts of amounts on deposit in a U.S. bank,¹⁰⁸ whether by check drawn on a U.S. bank account or by electronic transfer of funds from one U.S. bank account to another U.S. bank account, are taxable gifts of tangible personal property. It is less clear whether a check drawn on a U.S. bank account but deposited in a foreign bank account for the donee or whether the payment of funds from an NRA's foreign bank account to a U.S. bank account would be a gift of currency made within the United States. To avoid the risk that a cash gift has U.S. situs, structure such gifts by an NRA from his or her foreign bank account to the donee's foreign bank account. Alternatively, the donor might purchase securities or other assets with the intended cash gift and make gifts of those assets to the donee. It is possible that the IRS could assert such gifts are taxable under the step-transaction doctrine if the donee sells the assets shortly after the gift and retains the sales proceeds.¹⁰⁹

iii. GST Tax Rules

Very generally, the GST tax is a separate regime which imposes tax with respect to certain transfers during life, at death, or from trusts which skip a generation. The GST tax applies to transfers at death or by gift by an NRA to the NRA's grandchildren or other individuals assigned to a generation more than one generation removed from the NRA's own generation.¹¹⁰ The GST tax applies to such transfer by an NRA only if the transferred property is deemed to be situated in the United States for U.S. gift or estate tax purposes.

c. U.S. Transfer Tax Treatment of Nonresident Aliens

i. Estate Tax

The estate of an NRA must file a federal estate tax return if the decedent's U.S. gross estate exceeds \$36,000.¹¹¹ The rates of tax on an NRA's estate are identical to those for citizens and resident aliens.¹¹²

The U.S. estate and GST taxes were effectively repealed for 2010. The estate and GST taxes were reinstated in 2011 to provide a \$5 million exemption for U.S. citizens and domiciliaries and a maximum tax rate of 35% for deaths occurring or transfers made in 2011 and 2012.¹¹³ The American Taxpayer Relief Act of 2012, enacted on January 2, 2013 permanently increased the estate and gift tax exemption to \$5 million (indexed for inflation) and set the top rate at 40%.¹¹⁴ For 2016, the exemption amount is \$5.450 million per person or \$10.900 million for a couple.

Absent treaty benefits, an NRA's estate is entitled to a credit of only \$13,000, sheltering \$60,000 of property from estate tax and the total value of the decedent's assets exceeding such amount is subject to the same graduated rates as U.S. decedents.¹¹⁵ This amount is not indexed for inflation. To the extent provided by treaty, the credit allowed is equal to the amount that bears the same ratio to the applicable credit amount as the value of the NRA's U.S. situs assets to the NRA's worldwide assets.¹¹⁶ In order to qualify for the marital deduction for property passing to a spouse, the Section 2056 requirements must be satisfied, and if the spouse is not a U.S. citizen, additional

requirements must be met, as discussed herein. An estate tax charitable deduction is allowed but only for bequests to U.S. charities or for use in the United States.¹¹⁷

A person who acquires property from an NRA generally takes a stepped-up basis in the property equal to the fair market value of the property at the date of the decedent's death, regardless of whether the property was includable in the NRA's gross estate.¹¹⁸ In certain situations, the step-up is not allowed unless the property was includable in the NRA's gross estate, regardless of whether estate tax was actually payable.¹¹⁹ However, property acquired from a non-U.S. domiciliary is eligible for a \$60,000 increase only, but such basis may not be increased by built-in losses or loss carryovers.¹²⁰

ii. Gift Tax

The rates of tax on lifetime transfers by an NRA are the same as the rates for such transfers by U.S. domiciliaries and resident aliens. An NRA is entitled to the benefit of the annual exclusion for transfers of a present interest in property which for 2015 is \$14,000 per donee. A gift of \$148,000 (for 2016) to a noncitizen spouse of tangible personal property within the United States will not be subject to gift tax.¹²¹ A gift qualifies for this exclusion if it passes a present interest and would otherwise qualify for the marital deduction for lifetime gifts if the donee spouse were a U.S. citizen. For example, if a gift is made to a trust for the benefit of a non-citizen spouse that does not provide that spouse with *Crummey* powers, the gift may be excluded only to the extent of the present value of the non-citizen spouse's income interest.¹²²

An NRA donor may not take advantage of "gift splitting" with the donor's spouse under Section 2513. In addition, an NRA donor is not entitled to any unified credit against his gift tax liability.¹²³ An NRA is not entitled to a gift tax charitable deduction for gifts made to charities unless the charities are organized in the U.S. or the funds are for use in the United States.¹²⁴

A donee who acquires property from an NRA generally takes a basis in the property equal to the NRA's basis in the property.¹²⁵

iii. Will the Client Have Treaty Benefits? Dual Citizens: Impact of Treaties

If a non-U.S. domiciliary resides in a country with which the United States has an estate or gift tax treaty, the individual may have transfer tax planning opportunities that would not otherwise be available. Currently, the United States has 15 estate and/or gift tax treaties in force.¹²⁶ Treaties often provide relief from double estate and/or gift taxation by giving one country priority to tax property located in that country or to tax the estate or the gifts of a person based upon his or her domicile. Treaties that entered into force before 1971 are situs based, whereas those after 1971 are domicile based.

Before giving advice to a client who resides in any of the listed treaty countries, the advisor must carefully review the particular treaty (and protocols) involved, as each treaty has unique provisions, some of which are quite subtle. For example, a treaty will have its own definition of when a person is deemed to be domiciled in one of the partnering countries, which property may

be taxed by the country in which the property is situated, and how deductions for debts with respect to property are allowed. It is also important to remember that treaties generally limit benefits to persons with connections to the treaty country and not merely citizens or nationals.

Treaties generally apply only if a decedent's estate or beneficiaries will be subject to unlimited estate or inheritance tax in the treaty partner country. The careful advisor should consult with local counsel on treaty issues.

C. Will Property Transferred to a Spouse be Subject to U.S. Transfer Taxes?

Generally, the United States does not allow a marital deduction for gifts and bequests to noncitizen spouses.¹²⁷ For this purpose, it is immaterial whether the noncitizen spouse is a U.S. resident or an NRA. In contrast, a marital deduction is available to an NRA for gifts and bequests to a U.S. citizen spouse to the same extent as a U.S. citizen or resident donor.

a. Lifetime Transfers

While the lifetime transfer of any assets to a U.S. citizen spouse receives an unlimited marital deduction from the U.S. gift tax, the outright transfer of U.S. situs assets to a noncitizen spouse does not qualify for the marital deduction for U.S. gift tax purposes. There is no provision comparable to those for testamentary QDOTs.¹²⁸ Consideration should be given as to whether planning should be undertaken to have more assets in the name of the non-U.S. citizen spouse's name, particularly if he or she may ultimately leave the United States. Equal consideration should be given to the non-tax consequences in this type of planning, such as divorce or creditor protection. It may also be advantageous for any foreign real estate to be transferred to the non-U.S. citizen spouse so as to avoid the QDOT rules for large estates. A major word of warning should be remembered when considering transfers of foreign property between spouses, whether by inter vivos or testamentary gift. In some countries, such as Canada, the lifetime transfer by one spouse to the other will be subject to nonrecognition treatment for income tax purposes under law only if both are Canadian residents at the time of transfer. On the other hand, a testamentary gift of Canadian property to a surviving spouse will not be subject to Canadian income tax.

Lifetime transfers to noncitizen spouses are subject to a special "annual exclusion" provision that limits such gifts to an inflation-adjusted amount of \$148,000 (2016) per year. Such lifetime gifts may be used in planning to free the noncitizen spouse of the QDOT restrictions on these assets.

Unlimited gifts made by a U.S. citizen spouse to his or her noncitizen spouse in joint tenancy with right of survivorship or tenancy by the entirety will not be subject to gift tax at the time of the gift, although they may be subject to gift tax upon a future event (e.g. sale, withdrawal). Nevertheless, upon the death of the U.S. citizen spouse, the assets that were the subject of this form of gift will be subject to U.S. estate tax if the subject assets were deemed situated in the United States either at the transferor's death or at the date of the gift.¹²⁹

i. Gifts By a Spouse to Third Parties.

In some U.S. community property states, such as California and Washington, one spouse may not make a gift of community property without the consent of the other spouse.¹³⁰ In other states, gifts by one spouse of excessive amounts of community property may be void or voidable and possibly incomplete for gift tax purposes.¹³¹ If a gift of community property is made to a third party, the gift is treated as made one-half by each spouse.¹³² Spouses can agree on their rights to make gifts in premarital and post marital agreements. Spouses are permitted to split gifts for gift tax purposes, even though only one spouse contributed the gift property.¹³³ However, if either spouse is a non-U.S. domiciliary, gift splitting is not allowed.

ii. Gifts Between Spouses.

Since 1982, the gift tax marital deduction has been unlimited for transfers by gift between spouses. Further, no gift tax is incurred if one spouse converts separate property into community property by gift or transmutation. However, no gift tax marital deduction is allowable for transfers of U.S. situs assets by gift to a non-U.S. citizen spouse.¹³⁴ The annual exclusion for lifetime gifts to a non-citizen spouse is currently \$148,000.¹³⁵ No gift tax return is required to be filed for the annual gift tax exclusion for gifts to a non-U.S. citizen spouse, provided the gifted amount does not exceed the annual exclusion amount.¹³⁶

Special attention should be given when planning for gifts to non-citizen spouses who are not domiciled in the United States so as to limit the assets of the donee spouse's estate that could be subject to U.S. estate tax. Gifts of assets that do not have a U.S. situs may be ideal for these purposes since they are not includable in the donee spouse's estate (e.g., shares of foreign corporation, foreign real estate).

Planning for gifts between spouses often includes avoidance of claims by creditors of the donee spouse and for minimizing estate taxes. Careful consideration must be given as to whether a couple's estates should be equalized for these purposes since the surviving spouse will lose a stepped-up basis in his or her one half of community property upon the death of the first spouse.¹³⁷

b. Transfers Upon Death

i. Basic Rules for the Marital Deduction for Estate Tax Purposes

A marital deduction is not allowed for property passing from a decedent to his or her noncitizen spouse at the decedent's death unless one of two exceptions applies. These rules assure that assets that pass free of tax for the benefit of a surviving noncitizen spouse will ultimately be subject to U.S. estate tax upon the surviving spouse's death.

The first exception permits a marital deduction if the surviving spouse becomes a U.S. citizen before the deceased spouse's federal estate tax return is filed.¹³⁸ In addition, the surviving spouse must have been a U.S. resident at all times after the death of the deceased spouse and before becoming a U.S. citizen, no tax may have been imposed with respect to any distributions from a qualified domestic trust ("QDOT") before the spouse becomes a citizen or the surviving

spouse must have elected to treat any QDOT distributions on which tax was imposed as a taxable gift from the deceased spouse (thereby reducing the credit allowed under Section 2505).¹³⁹ As a practical matter, it may be quite difficult for the surviving spouse to acquire U.S. citizenship within the requisite timeframe, unless the process is already underway at the time of the decedent's death. The second exception allows a marital deduction if the property passes from the deceased spouse to a QDOT.¹⁴⁰

ii. Use of a QDOT

The property passing to a QDOT must be transferred to the QDOT before the deceased spouse's federal estate tax return is filed or the property is irrevocably assigned to a QDOT before the return is filed.¹⁴¹ To qualify for the marital deduction, a QDOT must otherwise comply with the general marital deduction requirements, specifically entitling the surviving spouse to all of the income from the trust by way of a life estate with a power of appointment, a QTIP trust, a charitable remainder trust or meeting the requirements of an estate trust.¹⁴² It must also permit principal distributions only to the surviving spouse, require that at least one trustee be an individual U.S. citizen or domestic corporation,¹⁴³ and give the U.S. trustee the power to withhold the estate tax that may be imposed on any principal distribution from the trust. In addition, the executor must make a timely, irrevocable QDOT election.¹⁴⁴ No election may be made on a return filed more than one year after the time prescribed for filing the return, including extensions.¹⁴⁵ The QDOT to which such property is transferred may be one previously established by the deceased spouse, one created by the decedent's executor or one created by the surviving spouse to transfer or irrevocably assign property he or she receives after the deceased spouse's death.¹⁴⁶

Only property owned by the deceased spouse may be transferred to the QDOT; thus, it may not include the surviving spouse's interest in any community property asset. For example, if only a portion of a property interest in joint tenancy property by application of the rules under Section 2010(a) is includable in the deceased spouse's estate, only that portion may be transferred to the QDOT.

It is also possible to reform a QDOT. Reformation may enable the surviving spouse to exercise a power to withdraw assets from the trust and treat the transfer as an outright transfer from the decedent. A reformed trust may be revocable by the surviving spouse or subject to his or her general power of appointment, provided that no person, including the surviving spouse, has the power to amend the trust in a way in which it would no longer qualify as a QDOT. A nonjudicial reformation must be completed by the deadline for filing the decedent's federal estate tax return, including extensions. Even an irrevocable trust, such as a QTIP trust, may be reformed by judicial reformation if the reformation is completed by the filing due date for the decedent's return, irrespective of the date the return is actually filed. However, the trust must be treated as a QDOT prior to the time the judicial reformation has been completed.

Estate tax is payable from principal distributions from the QDOT to the noncitizen spouse.¹⁴⁷ The estate tax is based on the *decedent's* tax bracket.¹⁴⁸ Distributions of income from a QDOT are not subject to estate tax.¹⁴⁹ Distributions of principal on account of "hardship" are not subject to estate tax.¹⁵⁰ The determination of "hardship" is a question of fact. Under the Regulations, a distribution made in response to an immediate and substantial financial need

relating to the spouse's health, maintenance, education or support, or such needs for any person that the surviving spouse is legally obligated to support, will satisfy the hardship exception.¹⁵¹ The spouse must use liquid assets available to him or her outside of the QDOT before the hardship exception will apply.¹⁵²

If the QDOT consists of \$2 million or more of assets, other than a personal residence and related furnishings with a value of up to \$600,000, and without reduction for any indebtedness with respect to the assets as of the decedent's date of death¹⁵³, the trust instrument establishing the QDOT must include provisions that will allow the trustee to comply with additional security requirements to ensure the collection of the estate tax.¹⁵⁴

The trust instrument can allow the trustee of such QDOT to choose from one of these alternate security arrangements:

- (i) The trust instrument can require a U.S. bank (as defined in Section 581) to act as trustee;¹⁵⁵
- (ii) The trust instrument can require the trustee to post a bond in an amount equal to 65% of the value of the QDOT assets as of the decedent's date of death; or¹⁵⁶
- (iii) The trust instrument can require the trustee to furnish a letter of credit issued by a bank to the IRS for an amount equal to 65% of the fair market value of the QDOT's initial assets.¹⁵⁷

The trust instrument can allow for the trustee to choose among these options and to switch among them.¹⁵⁸

If the QDOT assets, without reduction for any indebtedness relating to the assets, have a value of \$2 million or less (excluding a personal residence and related furnishings with a value up to \$600,000), the trust instrument must provide that either no more than 35% of the fair market value of the trust assets, determined annually on the last day of the tax year, will consist of real property located outside of the United States, or that the trust will satisfy the above security requirements.¹⁵⁹

The Regulations contain extensive rules relating to the additional security provisions and allow a trust instrument to incorporate the rules by reference.¹⁶⁰

The QDOT election must be made by the executor on the decedent's estate tax return, and once made is irrevocable.¹⁶¹ As noted above, no election may be made on any return filed more than one year after the due date for the return, including extensions.¹⁶² If the trustee makes a distribution from a QDOT subject to estate tax, the trustee must generally file a Form 706-QDOT reporting the distribution and paying the tax on April 15 of the year following the year of the taxable distribution.¹⁶³

The remaining assets of the QDOT are taxable on the death of the surviving spouse. The tax is calculated as follows:

- (i) Calculate the estate tax resulting from the decedent's death—i.e., the tax based on the decedent's taxable estate, including prior adjusted taxable gifts, taxable transfers at death, and prior taxable QDOT principal distributions.
- (ii) If the assets of the QDOT are includable in the surviving spouse's gross estate for estate tax purposes, the spouse's estate must calculate the resulting estate tax based on the surviving spouse's brackets, adjusted taxable gifts, and credits.
- (iii) If the QDOT assets are includable in the surviving spouse's gross estate, his or her estate will receive a full credit under Section 2013 (credit for tax on prior transfers) for the estate tax payable by reason of the surviving spouse's death.¹⁶⁴ The usual time and percentage limitations applicable under Section 2013 do not apply in this situation.¹⁶⁵

The net result is that the couple will pay death taxes on the QDOT assets at the highest marginal rate, whether that is the decedent's or the surviving spouse's rate. This approach also effectively deprives the surviving spouse of his or her applicable credit if he or she does not have sufficient assets outside of the QDOT to use the credit.

If an individual U.S. trustee has chosen a bond or letter of credit for the security arrangement and reports the QDOT has having assets of \$2 million or less, the marital deduction will be disallowed in full if there is an understatement of 50% or more absent a showing of reasonable cause and good faith.¹⁶⁶

Caution should be taken in drafting a QDOT, taking into consideration the rules applicable to foreign trusts, which impose stringent reporting obligations on U.S. beneficiaries and may subject the trust to additional U.S. taxes. For example, by appointing a foreign person as co-trustee of a QDOT, the trust can be treated as a foreign trust. By giving an NRA the power to veto trust decisions, withdraw assets or remove and replace a trustee, the trust can be deemed a foreign trust.¹⁶⁷

Consideration should be given to whether a QDOT election is advisable in a particular situation, keeping in mind that a QDOT is only a transfer tax deferral mechanism. The cost and expense of establishing and maintaining a QDOT, the necessary meticulous attention to the QDOT requirements, the potential appreciation of the assets and the loss of control that comes with the requirement of having a U.S. trustee for a QDOT, and reporting requirements are all factors to consider in weighing the benefits versus the burdens of a QDOT. All in all, depending upon the circumstances, advisors often opt in favor of avoiding a QDOT.

An estate tax treaty may provide adequate relief from taxes through the allowance of a credit in lieu of a QDOT election, such as that provided under the U.S.-Canada tax treaty,

depending upon the size of the decedent's estate. In such cases, the treaty benefits may outweigh the QDOT election since in such case, the assets qualifying for the marital deduction will never be subject to U.S. transfer tax. If the treaty benefit is claimed, the executor cannot also make a QDOT election.¹⁶⁸ Alternatively, payment of the tax may be more desirable than establishing and maintaining a QDOT so as to give the surviving spouse more freedom to leave the United States without burdening him or her with the U.S. transfer tax system (subject to Section 877A expatriation issues that may apply).

A QDOT may also be unnecessary for certain German Nationals. Under the U.S.-Germany Estate and Gift Tax Treaty (the "German Treaty"), property, other than community property, that passes to the surviving spouse from a deceased spouse who was domiciled in, or a citizen of Germany, and which is subject to tax in the United States solely as a result of situs taxation in Germany (such as in the case of real estate) is includable in the decedent's U.S. estate only to the extent that its value exceeds 50% of the value of all property included in his U.S. taxable base.¹⁶⁹ In addition, the German Treaty allows a full marital deduction equal to the lesser of the applicable exclusion amount (without regard to any gifts previous made by the decedent) or the value of property that would qualify for the marital deduction if the surviving spouse had been a U.S. citizen.¹⁷⁰ To qualify for this treatment, the decedent must have been domiciled in Germany or the United States at the time of death, the surviving spouse must have been domiciled in Germany or the United States at such time, or if both the decedent and the surviving spouse were domiciled in the United States at such time, at least one of them must have been a German citizen.¹⁷¹ A prorata credit is allowed under the German Treaty equal to the greater of (i) a proportionate share of the unified credit then in effect for U.S. residents based on a fraction of the property of the decedent situated in the United States over the worldwide property of the decedent and (ii) the unified credit allowed to the estate of a NRA under U.S. law.¹⁷² An executor who elects benefits under the German Treaty must waive the benefits of any federal estate tax deduction under U.S. law on an estate tax return filed by the deadline for making a QDOT election.¹⁷³

There are special rules for annuities and other arrangements that cannot be assigned under federal, state or foreign law, which allow such assets to be treated as passing to a QDOT if the surviving spouse exercises one of two options with respects the "corpus portion" of the annuity or other arrangement.¹⁷⁴ Under the first option, the surviving spouse must agree to pay the deferred QDOT tax annually on the corpus portion of each annuity or arrangement payment that the surviving spouse receives. Under the second option, the surviving spouse must agree to transfer or roll over the corpus portion of each payment to a QDOT within sixty days of the surviving spouse's receipt of the payment.¹⁷⁵ However, to the extent that all or a part of the corpus portion of the annuity or other arrangement would be eligible for a hardship exemption if paid from a QDOT, a corresponding portion of the payment is exempt from the payment or rollover requirements.¹⁷⁶

iii. Portability and Non-Citizen Spouses

Section 2010 allows the estate of a decedent who is survived by a spouse to make a portability election, allowing the surviving spouse to apply the decedent's "deceased spouse unused exclusion amount" ("DSUEA") to the surviving spouse's own transfers during life and at

death. Portability generally permits a surviving spouse to use the most recent deceased spouse's DSUEA so as to avoid the loss of a first-to-die spouse's remaining exemption.¹⁷⁷

However, portability is not available to all decedents and the availability of the portability election will depend upon the citizenship of the decedent spouse. The unified credit of a nonresident non-citizen is not governed by Section 2010; rather, Section 2011 imposes the federal estate tax on U.S. assets of a non-U.S. citizen who is not a resident of the United States. No portability amendment was made to Section 2011. An executor of a nonresident non-citizen decedent's estate may not elect portability on behalf of that decedent.¹⁷⁸ Further, the estate of a nonresident non-citizen surviving spouse may not take into account the DSUEA amount of his or her last deceased spouse, except to the extent a treaty applies.¹⁷⁹

Special portability rules apply when property passes to a non-citizen in a QDOT. The amount of the deceased spouse's DSUEA amount cannot be calculated until the death of the surviving spouse or when the QDOT makes its final distribution and terminates.¹⁸⁰ As a result, a non-citizen surviving spouse for whom a QDOT was created will only be able to use the DSUEA amount from the deceased spouse against the surviving spouse's estate tax liability. Generally, the non-citizen surviving spouse cannot use the deceased spouse's DSUEA as part of his or her own exclusion amount for lifetime transfers unless the gift is made before he or she dies, or the QDOT terminates in a year before the year of his or her death. In the case where the QDOT terminates during the non-citizen surviving spouse's lifetime, then the DSUEA amount can be used by the surviving spouse for gift tax purposes after the termination date.¹⁸¹

iv. Use of Foreign Tax Credit

The estate of a U.S. citizen or resident decedent is entitled to claim a credit against estate tax for foreign death taxes actually paid to another country with respect to property located in that country.¹⁸² A credit is allowed for death taxes imposed by a foreign country that are substantially equivalent to an "estate, inheritance, legacy, or succession tax."¹⁸³ In essence, the tax must be imposed on the value of property (as opposed to the appreciation) transferred by a decedent to a beneficiary. As a practical matter, local counsel should be engaged to determine whether the taxes, including those imposed by political subdivisions, are imposed on the transfer of property at death.

The credit for foreign death taxes is subject to two computational limits, which are designed to (a) limit the credit to the taxes attributable to the property located in the foreign country imposing the tax and (b) to limit the credit to the proportion that the foreign property bears in relation to the total gross estate less the charitable and marital deduction. The credit is limited to the lesser of the amounts calculated under the two limitations.¹⁸⁴

The first limitation limits the credit to the product of (a) the foreign death tax paid to the particular foreign country and (b) the ratio of foreign property both situated in that country and included in the gross estate to the value of all foreign property subject to foreign death taxes in that same jurisdiction. For purposes of this limitation, the location of such property is generally determined under the principles used to determine the situs of property owned by a decedent who is nonresident not a citizen.¹⁸⁵ The foreign property and death tax paid is based on foreign values converted into U.S. dollars using the exchange rate in effect as of the date of valuation and payment

respectively.¹⁸⁶ If death taxes are imposed by two or more foreign countries this limitation must be calculated separately for each country. Further, if a foreign country imposes more than one kind of death tax or imposes taxes at different rates, such amounts are to be calculated separately and totaled to determine the first limitation for that country.

The second limitation limits the credit to the product of (a) the federal estate tax less the applicable credit and (b) the ratio of the value of foreign property that is both subject to tax in a foreign country and included in the gross estate to the value of the decedent's entire gross estate less any marital and charitable deduction. Unlike the first limitation, the second limitation uses the federal estate tax values of the foreign property.

Care should be taken in drafting testamentary documents to specifically direct that specific bequests to a surviving spouse be funded with property not subject to foreign tax. If a fractional share formula is used to fund a marital trust, any assets that will be taxed by a foreign jurisdiction should be disposed of so they will not qualify for the marital deduction.¹⁸⁷

c. Problems with Joint Property Interests Held by Spouses

Joint tenancy with rights of survivorship and tenancy by the entirety are common methods of titling assets for married individuals. Generally, property owned by spouses is assumed to be owned one-half by each spouse.¹⁸⁸ However, special rules apply to the creation and termination of joint interests between spouses when one or both spouses are not U.S. citizens.

i. Estate Tax Treatment

In general, section 2040(b) provides that half of the value of a property jointly owned is included in the estate of the predeceasing tenant of a "qualified joint interest." An interest so qualifies only if the only co-owners are spouses and there is a right of survivorship. Note that the definition of a "qualified joint interest" also includes "tenants by the entirety" property.

Section 2040(b) does not, however, apply to property owned jointly with a right of survivorship if the surviving spouse of the decedent is not a U.S. citizen.¹⁸⁹ Accordingly, the total value of such property is includable in the first decedent's estate for estate tax purposes except to the extent the executor can substantiate the contributions of the surviving spouse to the acquisition of the property. This may require complex accounting to trace contributions made by each spouse. In the case of community property, one-half of the community property is included in the deceased spouse's estate.¹⁹⁰ Where property was acquired jointly by gift, bequest or devise from a third party, only one-half of the property is included in the decedent's estate.¹⁹¹

ii. Gift Tax Treatment

The gift tax consequences of the creation or termination of a joint tenancy where there is a lifetime transfer by a donor to a noncitizen spouse generally depends on the character of property. In the case of *personal property*, the spouse who provided the funds to acquire the property will be treated as making a gift of half the value of the property to the noncontributing spouse on the creation of the joint tenancy.¹⁹² This rule applies, however, only to extent that gift tax principles

would treat the creation of the joint tenancy as a completed gift. For example, in many states the contributing spouse has the unilateral right to withdraw all the funds from the bank or brokerage account without the consent of the noncontributing spouse. In that event, the gift to the noncontributing spouse is complete only upon a withdrawal of funds by the noncontributing spouse. If severability of the tenancy may occur only by joint action of the parties, for example in a tenancy by the entirety, the amount of the gift is based on the parties' relative life expectancies.¹⁹³

If the property is *real property*, there is generally no gift on creation of the joint interest by a citizen and noncitizen spouse.¹⁹⁴ However, upon termination of the joint interest (for example upon sale), the donor spouse is deemed to make a gift to the extent that the proportion of the total consideration furnished by the donor spouse multiplied by the value of the proceeds on termination (whether in cash or property) exceeds the value of the proceeds of termination received by the donor spouse.¹⁹⁵

As discussed above, a gift by a spouse to a non-citizen spouse is eligible for the special annual exclusion. Following such gift, opportunities exist for the non-citizen spouse to avoid or minimize U.S. estate tax. First, if the non-citizen spouse resides in the United States at the time of the gift, he or she can avoid U.S. estate tax by removing the gifted property from the United States and establishing residence outside of the United States before his or her death. In addition, a non-citizen spouse who is a U.S. domiciliary may use his or her applicable exclusion amount to benefit his or her U.S. citizen spouse and thereby reduce the estate tax on property otherwise included in his or her estate. This advantage is not available for assets transferred to a QDOT. Also, if the non-citizen spouse does not reside in the United States at the time of the gift, he or she will avoid U.S. estate tax on the gift unless the gifted property has a U.S. situs at the non-citizen spouse's death. (e.g., a NRA noncitizen spouse of a U.S. citizen domiciled abroad).

There are other planning possibilities available to minimize U.S. estate tax with respect to lifetime gifts of jointly-held property to the non-citizen spouse. With planning for a U.S. citizen spouse to gift joint property to his or her non-citizen spouse over time, using the annual lifetime exclusion, gift tax may be avoided when the non-citizen spouse later sells or transfers the gifted property. As noted above, gift tax will be imposed to such transfers to the extent the non-citizen spouse receives proceeds in excess of his or her proportionate share of any contribution to acquire the property. But be careful to trace all assets when changing title to jointly held assets where one spouse is a non-U.S. citizen.

¹ See California Family Code §§ 297.5, 299. All references to the California Family Code are hereinafter referred to as "CA Fam. Code."

² Some states recognize a common law marriage (non-ceremonial or by agreement between the couple). Most of the community property states, including California, do not recognize common law marriages. Some states recognize such marriages from another state or foreign jurisdiction where the relationship was created.

³ *Charania v. Commissioner*, 133 T.C. No. 7 (2009); *aff'd*, 608 F3d 67 (1st Cir. 2010).

⁴ Internal Revenue Code §§ 1, 61. All section or § references are to the Internal Revenue Code of 1986 as amended ("IRC") or to the Treasury Regulations promulgated thereunder, unless otherwise indicated.

⁵ IRC § 7701(b)(1)(A).

⁶ IRC § 7701(b)(3)(A).

⁷ IRC § 7701(b)(3)(A)(ii).

⁸ Treas Reg § 301.7701(b)-1(c)(2)(i).

⁹ *Lujan v. Commissioner*, TC Memo 2000-365 (2000) (alien met Substantial Presence Test for both years at issue).

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- ¹⁰ IRC §§ 7701(b)(5)(A)-(E); Treas Reg § 301.7701(b)-3.
- ¹¹ IRC § 7701(b)(3)(i).
- ¹² IRC § 7701(b)(3)(B); Treas Reg § 301.7701(b)-2(b)(2)(a).
- ¹³ Treas Reg § 301.7701(b)-2(c)(1).
- ¹⁴ *Id.*
- ¹⁵ Treas Reg § 301.7701(b)-2(c)(2).
- ¹⁶ Treas Reg § 301.7701(b)-2(d).
- ¹⁷ IRC § 7701(b)(3)(C).
- ¹⁸ Treas Reg § 301.7701(b)-8.
- ¹⁹ IRC § 871(a).
- ²⁰ *Id.*
- ²¹ IRC § 871(a)(1)(A). NRAs and foreign entities, including foreign trusts, generally are not subject to the newly enacted 3.8% tax that applies to net investment income. IRC § 1411(e)(1); Prop Reg § 1.1411-3(b)(6). U.S. beneficiaries of foreign trusts may, however, be subject to the 3.8% net investment income tax. *See* Prop Reg § 1411(c)(3).
- ²² IRC § 1441(a).
- ²³ IRC §§ 871(h), 881(c)(2).
- ²⁴ IRC §§ 871(h)(3), 881(c)(3). With certain modifications, the section 318 attribution rules apply for purposes of determining a whether a foreign lender owns 10% or more of an entity paying the interest.
- ²⁵ IRC § 871(a)(1)(B).
- ²⁶ IRC § 871(a)(1)(D).
- ²⁷ IRC § 871(a)(2).
- ²⁸ IRC § 1441(c)(1).
- ²⁹ IRC § 871(b).
- ³⁰ IRC § 871(d).
- ³¹ IRC § 1441(a); Treas Reg § 1.1441-6.
- ³² IRC § 1461; Treas Reg § 1.1461-2(b).
- ³³ Treas Reg § 1.1461-1(b).
- ³⁴ Treas Reg § 1.1461-1(c)(1).
- ³⁵ Treas Reg § 1.1461-1(c)(1)(i).
- ³⁶ IRC § 1462.
- ³⁷ Treas Reg § 1.1441-(6).
- ³⁸ Treas Reg § 1.1441-7(b)(8)(ii)(A)(2).
- ³⁹ Treas Reg § 1.1441-4(b)(2)(ii).
- ⁴⁰ IRC § 1441(b).
- ⁴¹ Treas Reg §§ 1.1446-1(c)(2)(ii)(C), (E).
- ⁴² IRC § 873(a).
- ⁴³ IRC § 873(b).
- ⁴⁴ IRC § 63(c)(6).
- ⁴⁵ IRC § 2(b)(3)(A).
- ⁴⁶ Treas Reg § 1.1-1(a)(2)(ii).
- ⁴⁷ IRC §§ 871(b); 55.
- ⁴⁸ Treas Reg § 1.874-1. Upon establishing good cause in unusual circumstances, the filing deadline may be waived by the IRS. Treas Reg § 1.874-1(b)(2).
- ⁴⁹ Treas Reg § 1.874-1(b)(1).
- ⁵⁰ 126 TC 96 (2006).
- ⁵¹ 515 F3d 162 (3d Cir 2008).
- ⁵² Under the “*Golsen* rule”, the Tax Court follows the rule adopted by the Court of Appeals to which the taxpayer has a right of appeal. *Golsen v. Commissioner*, 54 TC 742 (1970).
- ⁵³ Treas Reg § 1.874-1(b)(6).
- ⁵⁴ United States Dep’t of Treasury, United States Model Tax Convention on Income, art. 7, ¶ 1, Sept. 20, 1996 (hereinafter 1996 U.S. Model Income Tax Treaty); OECD Committee on Fiscal Affairs, Model Tax Convention on Income and on Capital, art. 7, ¶ 1, 1995 (hereinafter 1995 OECD Model Income Tax Treaty).
- ⁵⁵ 1996 U.S. Model Income Tax Treaty, art. 5, ¶ 1; 1995 OECD Model Income Tax Treaty, art. 5, ¶ 1.
- ⁵⁶ 1996 U.S. Model Income Tax Treaty, art. 5, ¶ 2; 1995 OECD Model Income Tax Treaty, art. 5, ¶ 2.
- ⁵⁷ IRC § 6114; Treas Reg § 301.6114-1(d)(1).
- ⁵⁸ An Act to Provide for Reconciliation Pursuant to Section 3 of the First Concurrent Resolution on the Budget for the Fiscal Year 1981, Pub L No 96-499, 94 Stat 2599 (1980). *See* IRC § 897.
- ⁵⁹ *See* IRC § 897.
- ⁶⁰ *See* IRC § 897(c).
- ⁶¹ IRC § 897(j).
- ⁶² IRC §§ 897(c)(1); (2).

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- ⁶³ IRC § 897(c)(1)(B).
- ⁶⁴ IRC § 897(c)(3).
- ⁶⁵ IRC § 1445.
- ⁶⁶ IRC § 1445(a).
- ⁶⁷ Treas Reg § 1.1445-1(c)(1).
- ⁶⁸ Treas Reg § 1.1445-1(b)(1).
- ⁶⁹ Treas Reg § 1.1445-1(e).
- ⁷⁰ Treas Reg § 1.1445-1(c).
- ⁷¹ Treas Reg § 1.1445-3.
- ⁷² Treas Reg § 1.1445-1(f).
- ⁷³ Treas Reg § 1.1445-3(q).
- ⁷⁴ *Poe v. Seaborn*, 282 U.S. 101 (1930).
- ⁷⁵ See M. Berger Strickland, Comment, *What's Mine is Mine: Reserving the Fruits of Separate Property*, 51 Loy. L. Rev. 989, 996-99 (2005).
- ⁷⁶ Fam. Code § 770. Arizona, New Mexico, Nevada and Washington also follow this rule.
- ⁷⁷ These states are Idaho, Louisiana, Wisconsin and Texas.
- ⁷⁸ Treas Reg § 20.0-1(b).
- ⁷⁹ Treas Reg §§ 20.0-1(b); 25.2501-1(b).
- ⁸⁰ See *Bank of N.Y. & Trust Co. v. Commissioner*, 21 BTA 197 (1930), acq. 1931-1 CB 4, 67; *Jellinek v. Commissioner*, 36 TC 826 (1961), acq. 1964-1 CB 6; *Estate of Bloch-Sulzberger v. Comm'r.*, 6 TCM 1201, 1203 (1974); *Nienhuys v. Commissioner*, 17 TC 1149, 1159 (1952); *Estate of Paquette v. Comm'r.*, TC Memo 1983-571.
- ⁸¹ *Estate of Khan v. Commissioner*, T.C. Memo 1998-22 (1998).
- ⁸² *Id.*
- ⁸³ *Id.*
- ⁸⁴ Rev Rul 80-363, 1980-2 CB 249.
- ⁸⁵ Rev Rul 80-209, 1980-2 CB 248.
- ⁸⁶ 54 Fed Cl 590 (2002).
- ⁸⁷ *Id.* The court in *Jack* denied the taxpayer's motion for summary judgment and ordered trial to proceed on the determination of domicile.
- ⁸⁸ IRC §§ 2101, 2103, 2106.
- ⁸⁹ IRC §§ 2501(a)(1)–(2); 2511.
- ⁹⁰ IRC § 2103; 2031; Treas Reg § 20.2104-1(a)(1).
- ⁹¹ IRC § 2102; 2103; 2106; Treas Reg § 20.2104-1(a)(2).
- ⁹² IRC § 2104(c); Treas Reg §§ 20.2104-1(a)(7).
- ⁹³ IRC § 2104(a); Treas Reg §§ 20.2104-1(a)(5).
- ⁹⁴ See Rev Rul 55-701, 1955-2 CB 836; *Sanchez v. Bowers*, 70 F2d 715 (2d Cir 1934).
- ⁹⁵ IRC § 2106(b); *Estate of Fung v. Comm'r.*, 117 TC 247 (2001), *aff'd* 91 AFTR 2d 2003-1228 (9th Cir 2003).
- ⁹⁶ IRC § 2106(b); *Johnstone v. Commissioner (A)*, 19 TC 44 (1952), acq., 1953-1 CB 5.
- ⁹⁷ IRC § 2104(a); Treas Reg § 20.2104-1(a)(5).
- ⁹⁸ IRC § 2105(a); Treas Reg § 20.2105-1(g).
- ⁹⁹ *Sanchez v. Bowers*, 70 F2d 715 (2d Cir 1934).
- ¹⁰⁰ 277 US 1 (1928).
- ¹⁰¹ 1955-2 CB 836.
- ¹⁰² 70 F2d 715 (2d Cir 1934).
- ¹⁰³ IRC § 2104; Treas Reg § 20.2104-1(b).
- ¹⁰⁴ See TAM 9507044 (Feb 17, 1995).
- ¹⁰⁵ IRC § 2014.
- ¹⁰⁶ See IRC § 2501(a)(2).
- ¹⁰⁷ IRC §§ 2501(a); 2511. If the donor is an NRA who expatriated from the United States, then the gratuitous transfers to a U.S. donee will be subject to an income tax in the hands of the donee equal to the highest gift or estate tax rate. IRC § 2081.
- ¹⁰⁸ See IRS en. Cons Memo 36860 (Nov 24, 1976).
- ¹⁰⁹ See *DeGoldschmidt-Rothchild v. Comm'r.*, 168 F2d 975 (2d Cir 1948).
- ¹¹⁰ IRC § 2601 *et. seq.*
- ¹¹¹ IRC § 6018(a)(2).
- ¹¹² IRC §§ 2101(b); 2001(c).
- ¹¹³ This compared to a \$3.5 million exemption and a maximum tax rate of 45% in 2009.
- ¹¹⁴ HR 8, 112 Cong 2011–2013. For 2015, the inflation-adjusted exemption amount is \$5.43 million.
- ¹¹⁵ IRC § 2102(b).
- ¹¹⁶ IRC § 2102(b)(3).
- ¹¹⁷ IRC § 2106(a)(2).
- ¹¹⁸ See IRC § 1014(b).

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- ¹¹⁹ See IRC § 1014(b)(6)–(10); Treas Reg § 1.1014.2. This type of property includes property that was not acquired by bequest, devise or inheritance from the decedent, but rather acquired by reason of death on the termination of a life estate, joint tenancy or the exercise or non-exercise of a power of appointment (other than a general power of appointment exercisable by will). IRC § 1014(b)(9).
- ¹²⁰ IRC § 1022(b)(3).
- ¹²¹ IRC § 2523(i); Rev Proc 2014-61, IRB 2014-47.
- ¹²² Treas Reg § 25.2523(i)-1(d), Ex.3
- ¹²³ IRC § 2505(a).
- ¹²⁴ IRC § 2522(b). No gift tax exemption applies for gifts of art located in the U.S. for exhibition purposes. Treas Reg § 25.2511-3(b)(1).
- ¹²⁵ See IRC § 1015.
- ¹²⁶ Australia (estate); Australia (gift); Austria (combined estate and gift); Belgium (proposed form-estate); Canada (estate—terminated with respect to estates of decedents dying on or after 1-1-85; see U.S.-Canada Income Tax Treaty regarding application of estate and gift taxes); Denmark (combined estate and gift); Finland (estate); France (combined estate and gift); Germany (combined estate and gift); Greece (estate); Ireland (estate); Italy (estate); Japan (combined estate and gift); Netherlands (estate); Norway (estate); South Africa (estate); Sweden (combined estate and gift—terminated when Sweden abolished inheritance and gift tax); Switzerland (estate); and United Kingdom (combined estate and gift).
- ¹²⁷ IRC § 2056.
- ¹²⁸ IRC § 2523(a).
- ¹²⁹ IRC § 2523(i)(3) (The principles of former IRC §§ 2515 and 2515A (which were repealed in 1981) shall continue to apply to transfers by a U.S. spouse to a noncitizen spouse as far as tenancies by the entirety and joint tenancies with rights of survivorship are concerned).
- ¹³⁰ CA Fam. Code § 1100; Wash. Rev. Code § 26.16030(2).
- ¹³¹ *Kelly Est v. Commissioner*, 31 T.C. 493 (1958).
- ¹³² *Roeser v. Commissioner*, 2 T.C. 298 (1943), *acq.* 1943 C.B. 19.
- ¹³³ IRC § 2513.
- ¹³⁴ *Id* at 2523(i).
- ¹³⁵ *Id* at 2523(i)(2). This amount is adjusted for inflation annually.
- ¹³⁶ IRC §§ 6019, 2523(i)(2), 2503.
- ¹³⁷ *Id* at 1014(b)(6).
- ¹³⁸ IRC § 2056(d)(4).
- ¹³⁹ *Id.*
- ¹⁴⁰ IRC § 2056(d)(2)(A).
- ¹⁴¹ IRC § 2056(d)(2)(B).
- ¹⁴² IRC §§ 2056(b)(5), (7), (8); Treas Reg § 20.2056E-2(B)(i–ii).
- ¹⁴³ If the U.S. trustee is an individual, he or she must have a tax home in the U.S. as defined in IRC § 911(d)(3).
- ¹⁴⁴ IRC § 2056A(a)(d); Treas Reg § 20.2056A-2(b)(1).
- ¹⁴⁵ IRC § 2056A(d).
- ¹⁴⁶ IRC § 2056(d)(2)(B); Treas Reg §§ 20.2056A-2(b)(2), (3).
- ¹⁴⁷ IRC § 2056(A)(b).
- ¹⁴⁸ Treas Reg § 20.2056A-6(a).
- ¹⁴⁹ IRC § 2056A(b)(3)(A). Income does not include capital gain. Treas Reg § 20.2056A-(c)(2).
- ¹⁵⁰ IRC § 2056A(b)(3)(B).
- ¹⁵¹ Treas Reg § 20.2056A-5(c)(1).
- ¹⁵² *Id.*
- ¹⁵³ Treas Reg § 20.2056A-2(d). The residence may not be rented to third parties even if it is not in use.
- ¹⁵⁴ Treas Reg § 20.2056A-2(d)(1).
- ¹⁵⁵ Treas Reg § 20.2056A-2(d)(1)(A).
- ¹⁵⁶ Treas Reg § 20.2056A-2(d)(1)(B).
- ¹⁵⁷ Treas Reg § 20.2056A-2(d)(1)(C).
- ¹⁵⁸ Treas Reg § 20.2056A-2(d)(1).
- ¹⁵⁹ See Rev Proc 96-54, 1996-2 CB 386. A look-through rule is provided for entities owning foreign real property.
- ¹⁶⁰ Treas Reg § 20.2056A-2(d)(1).
- ¹⁶¹ Treas Reg § 20.2056A-3(a).
- ¹⁶² IRC § 2056A(d).
- ¹⁶³ IRC § 2056A(b)(5).
- ¹⁶⁴ IRC § 2056(d)(3).
- ¹⁶⁵ *Id.*; Treas Reg § 20.2056A-7.
- ¹⁶⁶ Treas Reg § 20.2056A(d)(1)(i)(D).
- ¹⁶⁷ Treas Reg § 301.7701-7(d)(4).
- ¹⁶⁸ Treas Reg § 20.2056A-1(c).

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- ¹⁶⁹ 1980 Estate, Inheritance, and Gift Tax Convention, as Amended, U.S.-Ger., art. 10 ¶ 4, Dec. 3, 1980 (hereafter German Treaty). Deduction is not available if the U.S. citizen spouse is domiciled in Germany. *Id.*
- ¹⁷⁰ *Id.* at art. 10(6).
- ¹⁷¹ *Id.*
- ¹⁷² *Id.* at art. 10(5).
- ¹⁷³ *Id.* at art. 10(6).
- ¹⁷⁴ Treas Reg § 20.2056A-1(a)(1)(iv); Treas Reg § 20.2056A-4(c).
- ¹⁷⁵ Treas Reg § 20.2056A-3(c)(3).
- ¹⁷⁶ Treas Reg § 20.2056A-4(c)(2)(i); Treas Reg § 20.2056A-4(c)(3)(i).
- ¹⁷⁷ IRC §§ 2010(c)(4), (5)(A).
- ¹⁷⁸ Treas Reg § 20.2010-2T(a)(5).
- ¹⁷⁹ Treas Reg §§ 20.2010-3T(e); 25.2505-2T(f).
- ¹⁸⁰ Temp Treas Reg §§ 20.2010-2T(c)(4), 20.2010-3T(c)(2), 25.2505-2T(d)(2).
- ¹⁸¹ Temp Treas Reg § 25.2505-2T(c)(2)(ii).
- ¹⁸² IRC § 2014.
- ¹⁸³ Rev. Rul. 82-82, 1982-1 C.B. 127 (ruling that a Canadian tax on capital gains was levied on the appreciation and not transfer of property at death).
- ¹⁸⁴ § 2014(b).
- ¹⁸⁵ § 2014(a); see IRC §§ 2104, 2105.
- ¹⁸⁶ Treas Reg § 20.2014-2(a); Rev. Rul. 75-439, 1975-2 C.B. 359.
- ¹⁸⁷ Treas Reg § 20.2014-3(b).
- ¹⁸⁸ IRC § 2040(b).
- ¹⁸⁹ IRC §§ 2040(a); 2056(d)(1)(B).
- ¹⁹⁰ IRC § 2033.
- ¹⁹¹ IRC § 2040.
- ¹⁹² IRC §§ 2503(b); 2523(a); 2523(i)(2); Treas Reg § 25.2523(i)-2(c)(1).
- ¹⁹³ Treas Reg § 25.2523(i)-2(c)(2).
- ¹⁹⁴ IRC § 2523(i)(3).
- ¹⁹⁵ Treas Reg § 25.2523(i)-2(b)(1).