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Estate Planning and Tax Considerations for Nonresident Aliens

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Estate planning is not just for U.S. citizens and residents. Many nonresident aliens face unique estate planning concerns if they own U.S. real estate or other property located in the U.S. that they wish to gift or transfer at the time of their death. Generally, nonresident aliens are noncitizens and nonresidents of the U.S. who may temporarily reside in the U.S., but have an intention to return to their home country. That is, they do not have a “domicile” in the U.S. for gift and estate tax purposes.

Transfer tax rules differ if a nonresident alien is making a gift or transferring assets at death. On one hand, a nonresident alien is subject to the gift tax on transfers of U.S. currency, real estate and tangible personal property located in the U.S. at the time of the gift. On the other hand, intangible property such as corporate stock and partnership interests are not subject to gift tax, but they may be taxed as part of the nonresident alien's estate at death.

Unlike an U.S. citizen or resident whose taxable estate includes their worldwide assets, the taxable estate of a nonresident alien includes only tangible and intangible property located in the U.S. (“U.S. situs assets”). For estate tax purposes, U.S. situs assets include real property, shares in a U.S. corporation, debt obligations of a U.S. person, interests in U.S. partnerships (based on a case-by-case determination) and interests in U.S. trusts. But most bank deposits in U.S. banks (an exception being cash accounts with brokerage firms) and the death benefit of an insurance policy, even if paid by an U.S. insurance company, are not considered U.S. situs assets and therefore are not taxed as part of a nonresident alien's estate.

While U.S. citizens and residents benefit from a current lifetime gift and estate tax exemption of \$11,400,000 (2019), nonresident aliens are only entitled to a \$60,000 exemption, with transfers at death that exceed this amount subject to an effective 40% federal estate tax rate. Several states have their own estate tax. In Massachusetts, if the nonresident alien's estate exceeds \$1,000,000, the estate tax rates range from 0.8% to 16%.

The estate of a nonresident alien is entitled to deductions for estate expenses by applying a ratio of U.S. situs assets in relation to total worldwide assets. However, the estate of a nonresident alien cannot defer estate taxes until the

surviving spouse's death by taking advantage of an unlimited marital deduction, which is only available when a decedent leaves assets to a surviving spouse who is an U.S. citizen or to a [qualified domestic trust \(QDOT\)](#).

The U.S. has estate and gift tax treaties with 15 countries: Australia, Austria, Denmark, Finland, France, Germany, Greece, Ireland, Italy, Japan, Netherlands, Norway, South Africa, Switzerland and the United Kingdom. These tax treaties can alter the above gift and estate tax rules for nonresident aliens with respect to domicile, situs and taxability of assets, and tax credits and deductions, and oftentimes can soften the harshness of the rules.

For example, the U.S. estate and gift tax treaty with Germany offers relief in at least three notable ways for a nonresident alien domiciled in Germany who dies owning U.S. situs property. First, certain assets – such as stock in an U.S. “C” corporation – that would otherwise be subject to U.S. estate tax are excluded from the gross estate of the nonresident alien. Second, the estate of the nonresident alien can benefit from an effective prorated federal estate tax exemption (the current \$11,400,000 exemption available to U.S. citizens, multiplied by a ratio of U.S. assets to worldwide assets), possibly providing relief from the highest marginal estate tax rate of 40%. Third, the treaty provides a marital deduction to the nonresident alien's estate that would otherwise be unavailable for assets passing to a surviving spouse who is a non-U.S. citizen.

Client Tip: Nonresident aliens with property interests in the U.S. should consult legal counsel to review whether a tax treaty can minimize the impact of gift and estate taxes in the U.S. Please contact the Estate, Financial and Tax Planning group for more information.