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Estate Planning for Mixed Nationality Couples

Key Issues and Strategies for Both the U.S. and Non-U.S. Spouse

Presented by:

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Estate Planning for Mixed Nationality Couples

- What transfer tax rules must be considered for mixed nationality couples?
- How do immigration and resident tax status impact planning opportunities?
- What issues arise for joint and separate ownership of assets?



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The Life Span of an International Executive

- H and W are citizens and residents of a foreign country where they started their careers and raised a family. They have some basic estate planning in place including some family trusts.
- In 1995, H receives a promotion and is transferred to head the company's U.S. operations.
- Prior travel to the U.S. has been minimal.
- H and W move to N.Y. and rent an apartment in an exclusive neighborhood in NYC. They maintain the residence in their home country as H and W intend to move back at the date of H's retirement. W does not work outside of the home.
- Initially, they live in the U.S. on temporary visas (L-1). However, for ease of travel they eventually apply for and receive lawful permanent residence status (a/k/a a U.S. green card). The green card has been renewed more than once.



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The Life Span of an International Executive (continued)

- In 2020, H became seriously ill. He retired from his job. H and W then moved back to their residence in their home country.
- The lease on the rented apartment in N.Y. was terminated and the financial assets were transferred back home. Only a moderate size retirement plan remained in the U.S.
- H and W continued to maintain their green cards after they left the U.S. To avoid an unplanned revocation of the green card, they applied for and were granted residency permits which allowed them to spend time abroad. They continue to file U.S. income tax returns.
- In 2021, H's father died.
- In 2022 (while still holding the green card), H died. He is survived by his wife and two adult children, all of whom are U.S. green card holders.
- The initial impression is that H died with total world wide assets valued at \$12,060,000. The only U.S. situs assets are valued at \$500,000.



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Pre-Immigration Strategies and Issues of Concern

- Draft a last will and testament
- Consider an ILIT
- Dispose of Passive Foreign Investment Corporations (PFICs)
- Consider check the box entity classification elections
- Complete any gifts
- Consider funding trusts



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Income Tax Residency

VS.

Estate Tax Residency



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**SCHEDULE B
(Form 1040)**

Department of the Treasury
Internal Revenue Service (99)

Interest and Ordinary Dividends

▶ Go to www.irs.gov/ScheduleB for instructions and the latest information.
▶ Attach to Form 1040 or 1040-SR.

OMB No. 1545-0074

2021
Attachment
Sequence No. **08**

Part III

You must complete this part if you **(a)** had over \$1,500 of taxable interest or ordinary dividends; **(b)** had a foreign account; or **(c)** received a distribution from, or were a grantor of, or a transferor to, a foreign trust.

**Foreign
Accounts
and Trusts**

Caution: If required, failure to file FinCEN Form 114 may result in substantial penalties. See instructions.

- | | Yes | No |
|---|-----|----|
| 7a At any time during 2021, did you have a financial interest in or signature authority over a financial account (such as a bank account, securities account, or brokerage account) located in a foreign country? See instructions | | |
| If "Yes," are you required to file FinCEN Form 114, Report of Foreign Bank and Financial Accounts (FBAR), to report that financial interest or signature authority? See FinCEN Form 114 and its instructions for filing requirements and exceptions to those requirements | | |
| b If you are required to file FinCEN Form 114, enter the name of the foreign country where the financial account is located ▶ _____ | | |
| 8 During 2021, did you receive a distribution from, or were you the grantor of, or transferor to, a foreign trust? If "Yes," you may have to file Form 3520. See instructions | | |



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Form **8938**
(Rev. November 2021)
Department of the Treasury
Internal Revenue Service

Statement of Specified Foreign Financial Assets

▶ Go to www.irs.gov/Form8938 for instructions and the latest information.

▶ Attach to your tax return.

For calendar year 20 or tax year beginning , 20 , and ending , 20

OMB No. 1545-2195

Attachment
Sequence No. 938

Part IV Excepted Specified Foreign Financial Assets (see instructions)

If you reported specified foreign financial assets on one or more of the following forms, enter the number of such forms filed. You do not need to include these assets on Form 8938 for the tax year.

15 Number of Forms 3520 <input type="text"/>	16 Number of Forms 3520-A <input type="text"/>	17 Number of Forms 5471 <input type="text"/>
18 Number of Forms 8621 <input type="text"/>	19 Number of Forms 8865 <input type="text"/>	



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U.S. Tax Treatment of Foreign Gifts & Inheritances

Foreign Gifts and Inheritances:

Reporting obligations

v.

Tax liability

There are opportunities for significant tax savings but the rules are complex and penalties are harsh

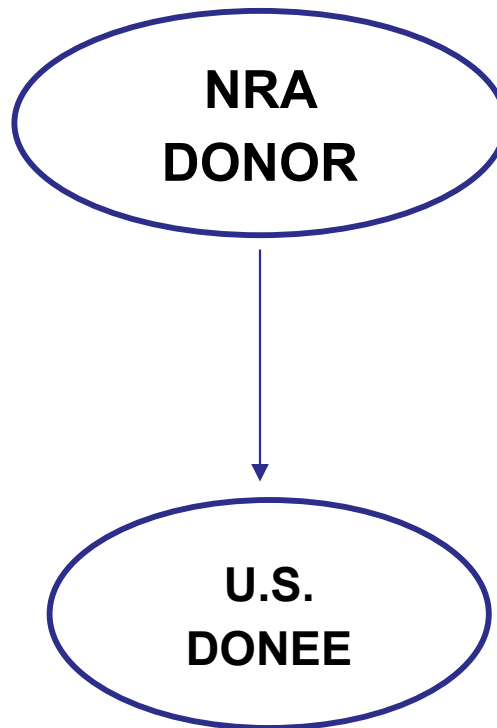


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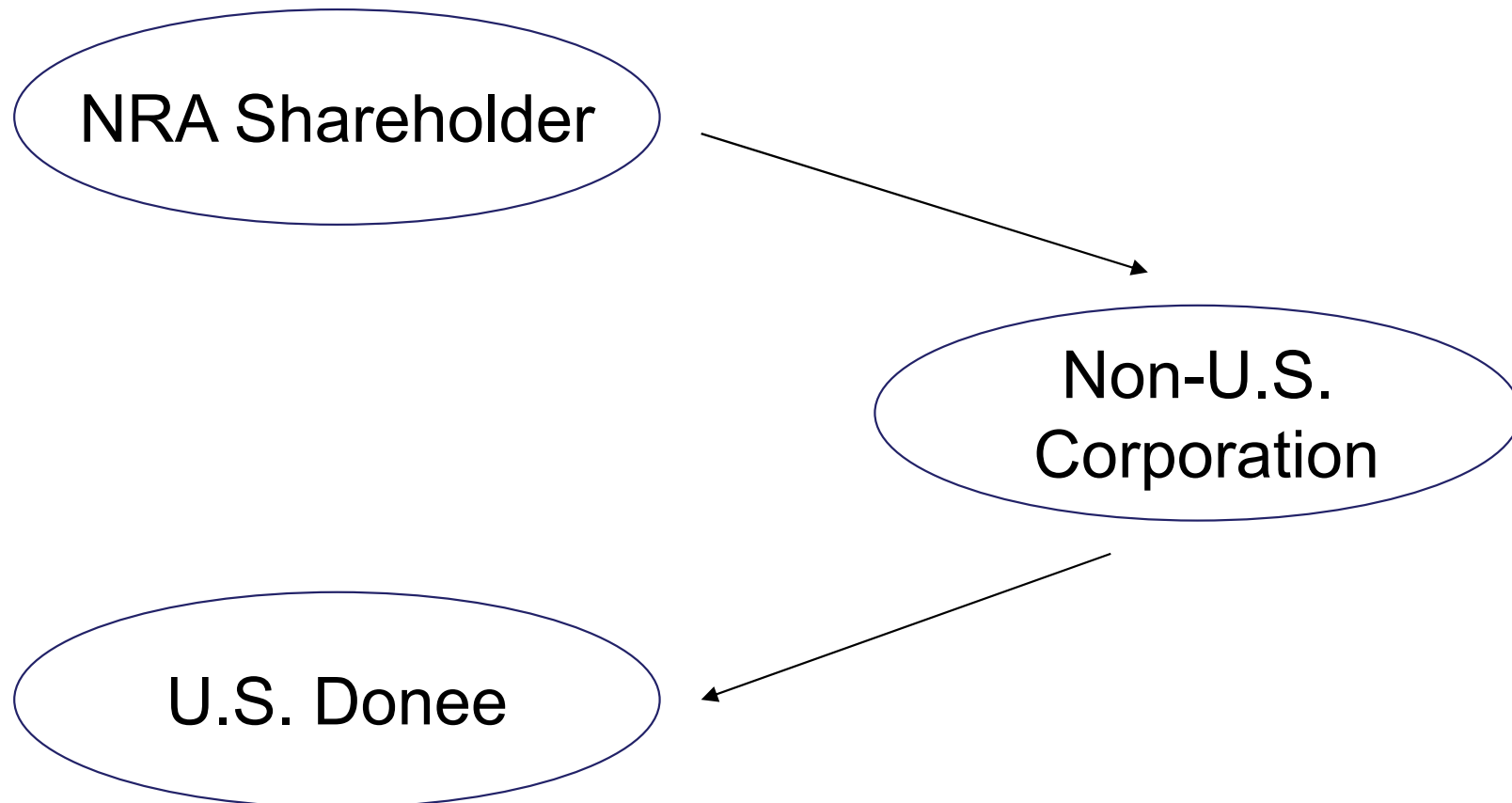
U.S. Tax Treatment of Foreign Gifts & Inheritances

An Actual Gift – example #1





A Purported Gift





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Income Tax Residency

VS.

Estate Tax Residency



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Estate Tax Residency

Resident defined for estate (and gift) tax purposes:

For estate tax purposes, a resident is someone who had a **domicile** in the United States at the time of death. A person acquires a domicile by living in a place for even a brief period of time, as long as the person had no intention of moving from that place. See Regulations section 20.0-1(b).

Estate of Jack v United States, 54 Fed. Cl. 590 (2002) held that a nonimmigrant visa is not conclusive evidence that the decedent was domiciled elsewhere.

Estate of Kahn v Commissioner, T.C. Memo 1998-22 – consider location of family.



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Estate Tax Residency

If the recipient spouse is not a U.S. citizen, there is no marital deduction.

Solutions to minimize the impact of no marital deduction include:

1. The Qualified Domestic Trust (QDOT)
2. In some cases, treaties provide relief



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U.S. Resident Transfer Tax Exemptions - 2022

- Annual gift tax exclusion - \$16,000
- Exclusion for gifts to non citizen spouse - \$164,000
- Estate and Gift Lifetime Exemption - \$12,060,000
- GST Exemption - \$12,060,000



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Estate Exemption Amounts

Non-Domiciliary Estates	Citizen or Domiciliary Estate
\$60,000	\$12,060,000
Limited to U.S. Situs Property (U.S. real estate, U.S. stock, retirement plans, etc.)	Worldwide property (everything)



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Administration of the Estate of H

- A position exists that he was not domiciled in the U.S. Form 706NA United States Estate (and Generation-Skipping Transfer) Tax Return Estate of nonresident not a citizen of the United States should be filed for the U.S. retirement plan.
- A position exists that the income tax residency of H's estate is also non-U.S. The U.S. concept of DNI applies but for this limited purpose it only includes U.S. sourced income.
- If the family trusts are Qualified Revocable Trusts, an IRC 645 election can treat the trust as part of the estate be made further lengthening the benefits of the special DNI rules for foreign estates. This election is made on Form 8855, Election to Treat a Qualified Revocable Trust as part of an estate.
- Tax identification numbers are required



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Administration of the Estate of H (continued)

- The assets included in H's estate under U.S. concepts are eligible for a step up in basis. Special trust rules apply. This does not apply for PFICs.
- If any of the lifetime trusts that were in place were "grantor trusts" under U.S. concepts would but not be included in a U.S. estate, then IRC 684 will apply, taxing the built-in appreciation in the trust assets on the date of death.
- Post death planning with a QDOT (if needed) can be done. However, QDOTs are really just a mechanism to defer the payment of the tax as opposed to an active tax savings strategy.
- Due care should be taken to make sure that all of the decedents foreign financial assets have been reported. The wording in the FATCA legislation of 2010 leaves open the possibility that the execution could be liable for any omissions.



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Estate Taxes:

The U.S. system for **NON** U.S. citizens

Estate of
NON U.S. Citizen
(U.S. Situs)
Non – domiciled
\$60,000 exemption

NO marital deduction



NON - U.S. Citizen
Surviving Spouse

\$500,000 nets \$150,000 appx
(after income tax & estate tax)



Kids

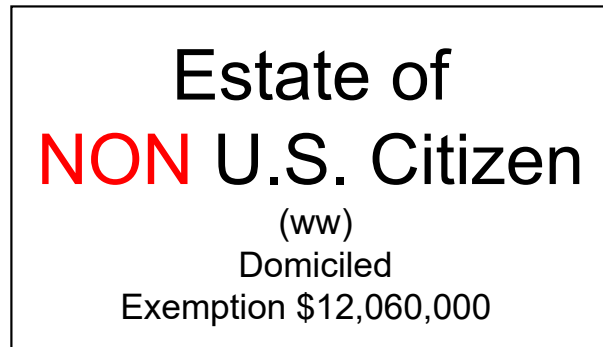


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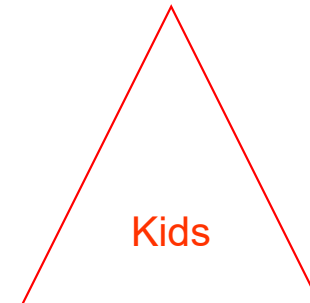
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Estate Taxes:

The U.S. system for **NON** U.S. citizens



NO marital deduction



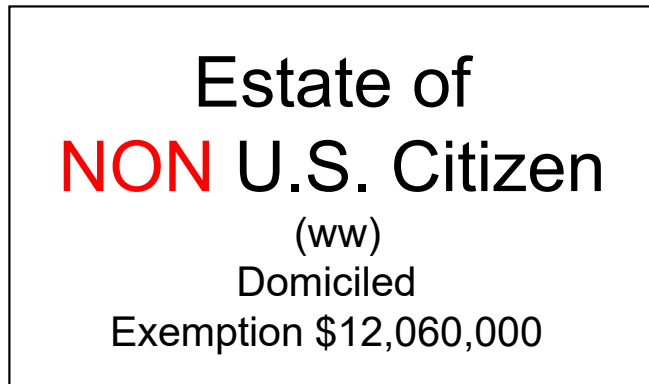


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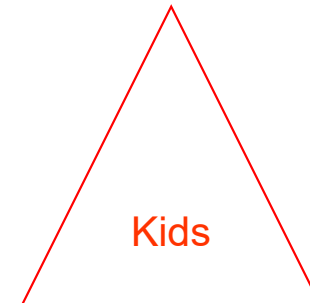
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Estate Taxes:

The U.S. system for **NON** U.S. citizens



NO marital deduction





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Marital Property Issues

- Separate property
- Joint property (with right of survivorship)
- Community property



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Technical Section

Income Tax Residency

Estate Tax Residency



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Income Tax Residency

Resident defined for income tax purposes:

A U.S. citizen,

A green card holder – lawful permanent residence status, or

A foreign national who has days of presence in the U.S. that meet the “substantial presence test” of IRC 7701 (a/k/a the 183 day/120 rule)



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Substantial Presence Test

- Under the substantial presence test a non U.S. person physically present in the United States under a weighed average formula for 183 days including partial days, is a U.S. income tax resident for that year.
- Under this “weighted average system” to satisfy the 183 days requirement, count:
 - (a) All of the days present in the current year, and;
 - (b) One-third (1/3) of the days present in the first year before the current year, and;
 - (c) One-sixth (1/6) of the days present in the second year before the current year.

For example, Sally Sample (“SS”) and John Doe (“JD”) are each present in the United States for various durations of time during the past three years.

	<u># of Days in the US</u>		<u>%</u>		<u>Total</u>	
	<u>SS</u>	<u>JD</u>	<u>SS</u>	<u>JD</u>	<u>SS</u>	<u>JD</u>
<u>2022</u>	120	183	100%	100%	120	183
<u>2021</u>	120	30	1/3	1/3	40	10
<u>2019</u>	120	0	1/6	1/6	<u>20</u>	<u>0</u>
					180	193

Despite being in the U.S. more days overall, SS does not pass the substantial presence test while JD does because of the weighted average rule.



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Residency Start Date

- For an individual treated as a non U.S. person for U.S. federal income tax purposes because of the substantial presence test, the “*residency start date*” is the first day present in the United States, provided that the individual can disregard up to **10** days of presence if the *closer connection test* is met during such ten-day period.
- The ten days cannot be part of a longer extended stay, and these rules do not affect the number of days actually counted for the substantial presence test.
- “Closer connection” is established by “more significant contacts.”
- Facts and circumstances to be considered include the location of the alien’s permanent home (immaterial whether a house, apartment or furnished room, or whether owned or rented, provided it is available to the alien at all times, continuously, and not solely for stays of short duration), family and personal belongings (such as automobiles, furniture, clothing, and jewelry owned by the alien or family); the location of social, political, cultural or religious organizations in which the alien is currently involved; the location where the alien conducts routine banking activities; the type of driver’s license held; the country of residence designated by the alien on various forms and documents, including official forms such as Form W-9; and where the alien votes.



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Residency Termination Date

- This is a similar concept to the residency start date.
- For the termination date, the taxpayer must satisfy the “close connection” with a particular country which may defer the termination date until the end of the year.
- Monitor future travel to avoid the anti-lapse rule.
- Dual status returns may be due in the years of departure and arrival.



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Exceptions

- Student visa
- Diplomatic visa
- Medical exceptions
- Closer connection (Form 8840)
- Treaty benefits (caution, informational forms may still apply)



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Traps for the Exceptions

- Capital gains
- Does not protect from gift tax, estate tax, and generation-skipping transfer tax
- Domicile vs. Non-domicile becomes important



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Preferred Status Visa - Tax Home Discussion

- Under “tax home” rules, a person who is away from his tax home for longer than 1 year has shifted tax homes to his new location upon his arrival in that new location.
- 30% tax imposed on U.S. source capital gains for nonresident alien individuals present in the U.S. for 183 days or more during taxable year
- Under this rule, most foreign alien employees of international organizations have shifted tax homes to the U.S. on the day of their arrival into the U.S., unless the particular program or employment clearly terminates in less than one year, they have no intention to remain in the U.S. after employment.



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International Charitable Giving

- Maximize your U.S. tax deduction
- Treaties may help