

Estate Planning Overview

Estate Planning with Cross Border Implications

International Tax Seminar

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Estate Planning with Cross Border Implications

A. Gift and Estate Taxes (effective 1/1/2011)

1. U.S. Citizens & Residents

- a. All Gratuitous Transfers of Money or Other Property, Whenever Located or Situated, are Subject to Gift or Estate Tax
- b. Gift Tax Imposed on Lifetime Transfers and Estate Tax Imposed on Testamentary Transfers Based on Fair Market Value of Property Transferred
- c. \$13,000 Gift Tax Annual Exclusion (Indexed for Inflation) and Medical/Tuition Gift Tax Exclusion for Lifetime Transfers
- d. Unlimited Marital and Charitable Deductions — Generally

Estate Planning with Cross Border Implications (Cont'd)

- e. Gift-Splitting By Spouses for Lifetime Gifts (But Only If Both Spouses are U.S. Citizens or Residents)
- f. Graduated Unified Estate and Gift Tax Rate Schedule Applicable to Taxable Gifts and Estates (See Appendix A)
- g. Cumulative Lifetime Gift Tax Exemption Amount — \$1,000,000
- h. Annual Gift Tax Returns – Generally Filed with Income Tax Returns — Tax Due 3-1/2 Months After End of Year (4/15)
 - (i) Tax Imposed on Donor
 - (ii) Tax-exclusive Calculation
(Based on net amount given to donee)

Estate Planning with Cross Border Implications (Cont'd)

i. Estate Tax Imposed on Decedent's Estate

- (i) Exemption Amount — \$1,000,000 (Reduced by Amount of Gift Tax Exemption Used)
- (ii) Tax-inclusive Calculation (Based on the Total Taxable Estate Including the Estate tax)
- (iii) Unified Lifetime and Testamentary Transfers (Adjusted Taxable Gifts)
- (iv) Credits for State Death Taxes, Gift Tax, Tax on Prior Transfers, Foreign death Taxes and Death Taxes on Remainders
- (v) Tax Prorated Among Taxable Beneficiaries (Generally Excluding Surviving Spouse & Charities)

Estate Planning with Cross Border Implications (Cont'd)

j. Transfers to Non-U.S.-Citizen Spouses

- (i) \$130,000 Gift Tax Annual Exclusion (Indexed for Inflation), but No Gift Tax Marital Deduction
- (ii) Qualified Domestic Trust — Estate Tax Marital Deduction
 - (A) All Income Payable Annually to Surviving Spouse
 - (B) Trustee Must Be U.S. Citizen or Corporation
 - (C) Estate Tax Payable on Distributions of Principal (During Spouse's Lifetime and Upon Spouse's Death)

k. Estate Tax Return for Transfers at Death — Tax Due 9 Months After Date of Death

Estate Planning with Cross Border Implications (Cont'd)

2. Non-Resident/Non-Citizen Donors and Estates

- a. Determination of Residence (Domicile)
- b. Only Transfers of Property Located or Situated in the U.S. are Taxable
- c. Lifetime Transfers — Gift Tax — Limited Application
 - (i) Real and Tangible Personal Property (Including Money) Situated in the U.S.
 - (ii) Not Applicable to Any Intangible Personal Property (Stock, Bonds, Partnership Interests, Promissory Notes, Etc.)
 - (iii) Annual and Medical/Tuition Exclusions

Estate Planning with Cross Border Implications (Cont'd)

- d. Testamentary Transfers — Estate Tax — Broader Application (Includes Stock of U.S. Corporation)
 - (i) Real and Tangible Personal Property (Including Money) Situated in the U.S.
 - (ii) Stock of U.S. Corporations
 - (iii) Debt Obligations of U.S. Persons (But Not Bank Accounts or “Portfolio” Debt Obligations, the Interest on Which Is Not Subject to U.S. Income Taxation)
- e. Gift and Estate Tax Exemptions
 - (i) No Lifetime Gift Tax Exemption Amount
 - (ii) Only a \$60,000 Estate Tax Exemption Amount
- f. Unlimited Marital and Charitable Deductions — Generally
- g. No Gift-Splitting Between Spouses

Estate Planning with Cross Border Implications (Cont'd)

B. The Generation-Skipping Transfer (“GST”) Tax

1. Applies Only to Transfers Subject to Gift or Estate Taxes
2. Applies Only to Transfers to or in Trust for the Benefit of Grandchildren or Other Beneficiaries in Generations More than One Generation Below the Transferor’s Generation
3. \$13,000 GST Tax Annual Exclusion
4. \$1,300,000 ± GST Exemption Amount
 - a. GST Exemption Allocated to ‘Direct Skips’ or to Generation-Skipping Trusts (Actual or Potential)
 - b. GST Trusts Generally Are Fully Exempt or Fully Subject to the GST Tax

Estate Planning with Cross Border Implications (Cont'd)

5. GST Tax Rate — Highest Gift and Estate Tax Rate — (55%)
6. Transfers Otherwise Subject to GST Tax Are Generally Subjected Instead to Gift or Estate Tax

C. Pre-Immigration Planning

1. Give Excess Assets to Children, Etc. Before Becoming a U.S. Citizen or Resident (Domiciliary)
 - a. Husband Might Establish an Irrevocable Trust for the Benefit of Wife and/or Issue (Wife Could Have Special Testamentary Power of Appointment Exercisable in Favor of Husband If she predeceases him)
 - b. Husband and Wife Might Establish an Irrevocable Trust for the Benefit of Their Issue

Estate Planning with Cross Border Implications (Cont'd)

D. Planning for Non-U.S. Citizens or Residents with U.S. Citizen or Resident Children, Etc.

1. The Non-US Citizen or Resident Should Own U.S. Situs Assets Through a Foreign Holding Company (e.g., a BVI Corp.)
2. He or She Might Establish Revocable Trusts for the Benefit of Each Child and His or Her Issue, with the Child as Trustee after Attaining a Mature Age
 - a. Non U.S. Situs Assets Could Be Owned Directly by the Trust
 - b. U.S. Situs Assets Should be Owned by, e.g., a BVI Corp. or Other Foreign Holding Company
 - c. Income (Including Capital Gains) Would Not Be Subject to Current U.S. Income Taxes
 - d. Assets Would Not Be Subject to U.S. Gift, Estate or GST Transfer Taxes on Death of the Non U.S. Citizen or Resident Parent

Estate Planning with Cross Border Implications (Cont'd)

3. Establish U.S. or Foreign Dynasty Trusts for the Benefit of Children and Their Issue On Death of Non U.S. Citizen or Resident Parent
 - a. A Child Could Be Trustee of U.S. Trust for the Benefit of Himself or Herself and His or Her Issue, with Appropriate Limitations on His or Her Rights and Powers as Trustee and Beneficiary
 - b. Foreign Trusts Could Avoid U.S. and CA Income Tax Throwback Rule If Accumulated Income Is Not Distributed to U.S. Beneficiaries
 - c. Trusts Would Be GST Exempt If Transfers Not Subject to U.S. Gift or Estate Taxes
 - d. Foreign Personal Holding Company ("FPHC") Assets Should Be Sold Periodically Before the Settlor's Death to Avoid Large FPHC Tax on Liquidation of Corp., and the Corp. Should Be Liquidated Within 30 Days After Death to Avoid Future FPHC Taxes

E. Departure Planning — U.S. Citizens and Residents (HEART Act)

Estate Planning with Cross Border Implications (Cont'd)

Appendix A

2011 FEDERAL UNIFIED ESTATE AND GIFT TAX RATE SCHEDULE

If the Taxable Estate or Taxable Gift is:		The Estate or Gift Tax is:		
From	To	Tax +	%	On Excess Over
\$ -0-	\$10,000	\$ -0-	18	\$ -0-
10,000	20,000	1,800	20	10,000
20,000	40,000	3,800	22	20,000
40,000	60,000	8,200	24	40,000
60,000	80,000	13,000	26	60,000
80,000	100,000	18,200	28	80,000
100,000	150,000	23,800	30	100,000
150,000	250,000	38,800	32	150,000
250,000	500,000	70,800	34	250,000
500,000	750,000	155,800	37	500,000
750,000	1,000,000	248,300	39	750,000
1,000,000	1,250,000	345,800	41	1,000,000 *
1,250,000	1,500,000	448,300	43	1,250,000
1,500,000	2,000,000	555,800	45	1,500,000
2,000,000	2,500,000	780,800	49	2,000,000
2,500,000	3,000,000	1,025,800	53	2,500,000
3,000,000	∞	1,290,800	55	3,000,000

* The applicable credit amount available as an offset to the estate and gift tax is \$345,800, which is equivalent to the tax on a taxable estate or gift of \$1,000,000

INTERESTS IN NON-GRANTOR TRUSTS

Unless the expatriate elects otherwise, §877A(f) provides for an automatic deferral of tax on the value of the expatriate's "interest in a non-grantor trust" — whether the trust is a domestic trust or a foreign trust. See IRS Notice 2009-85 (2009-45 IRS 598), §7.D).

If the expatriate does not elect otherwise, §877A(f)(4)(A) provides that rules similar to payments of "eligible deferred compensation" shall apply. Thus, the trustee must withhold 30% of the gross amount of the distribution (but §877A(f)(2) appears to limit the withholding to the amount of distributable net income attributable to the distribution.)

The expatriate's ongoing U.S. tax liability with regard to future distributions from a domestic trust is not limited to what the expatriate's tax would have been based on if the value of the expatriate's interest in the trust had been taxed at the time of expatriation.

There are no provisions for a foreign trust to "elect" to be treated as a U.S. trust for withholding tax purposes (in contrast with the rules on how the tax on the deferred tax on deferred compensation will be paid by a non-U.S. person). Thus, there is no mechanism for the IRS to directly enforce the requirement that the expatriate must report any tax due with regard to future distributions from a foreign trust.

NEW TRANSFER (“INHERITANCE”) TAX ON GIFTS AND BEQUESTS TO CERTAIN U.S. PERSONS

New IRC §2801(a) imposes a transfer tax on the fair market value of gifts or bequests of property situated anywhere in the world to a U.S. citizen or resident by an expatriate. The tax is imposed at the highest rate at which the federal estate or gift tax is imposed. The amount subject to tax has no relationship to the expatriate’s net worth at the time of expatriation.

Section 2801(d) provides for a “reverse foreign tax credit” equal to the amount of any gift or estate tax imposed on the gift or bequest by any foreign country. However, the transferee cannot claim the benefit of a reduction or elimination of the tax under an estate or gift tax treaty, because no existing treaty applies to inheritance type taxes imposed on a U.S. transferee.

The tax does not apply to property subject to U.S. gift or estate taxes shown on timely filed gift and estate tax returns, or to gifts that are excluded under IRC §2503(b) (and probably under IRC §2503(e), too). It also does not apply to qualifying transfers to a spouse or qualified charity.

The tax also is imposed on a gift or bequest by an expatriate to a domestic trust. A gift or bequest to a foreign trust is deferred until distribution is made from the trust to the U.S. citizen or resident beneficiary, and an income tax deduction is allowed under IRS §164 for the §2801 tax attributable to the portion of the distribution included in gross income. A foreign trust may elect to be treated as a domestic trust for purposes of §2801.

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Richard Kinyon designs and implements complex estate plans for high-net-worth individuals, including the establishment of various sophisticated irrevocable trusts and family investment companies, and he represents fiduciaries and beneficiaries in connection with the administration of estates and trusts, including litigation.

Mr. Kinyon advises closely held business owner clients on how to pass interests in their businesses to younger-generation family members and others in a tax-advantaged and creditor-protected manner. He also advises wealthy individuals on how to transfer their real estate, and other assets to the objects of their bounty.

Mr. Kinyon has lectured for numerous educational institutions, various local estate planning councils, and other organizations. He has authored chapters in California CEB treatises on drafting business buyout agreements, tax planning for the prospective retiree, using family partnerships as an estate planning tool, the income tax aspects of estates and trusts, "Dynasty Trusts" (in *Drafting California Irrevocable Trusts*), and "Overview of Estate Planning Practice" (in *California Estate Planning*). He also has written a number of articles for the *CEB Estate Planning & California Probate Reporter*, for which he also has served as guest editor, *Estate Planning*, *Trust & Probate NEWS*, and other professional journals.

Mr. Kinyon has been active in a number of professional organizations for which he has served as Chairman, including: the Committee on Tax Legislation & Regulations: Income Taxation of Trusts and Estates, of the Real Property, Probate & Trust Law Section of the American Bar Association; the Subcommittee on State Inheritance and Gift Taxes of the Estate Planning Committee of the Estate Planning, Probate, and Trust Law Section of the State Bar of California; and the Estate Planning, Trust, and Probate Law Section of the San Francisco Bar Association.

Mr. Kinyon has been recognized for his expertise in Trusts and Estate Planning by *San Francisco Magazine* as one of Northern California's "Super Lawyers." He has been a certified Specialist in Taxation Law by the California Board of Legal Specialization since 1973.

Mr. Kinyon attended Dartmouth College from 1957 to 1959, and received his B.A., *cum laude*, in 1961 and his LL.B., *cum laude*, in 1965 from the University of Minnesota. He served as Editor of the *Minnesota Law Review* from 1964 to 1965.