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Jennifer Jordan McCall and Christopher B Lacaria,Pillsbury Winthrop Shaw Pittman LLP

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TAXATION

Tax Year and Payment Dates

1. When does the official tax year start and finish in your jurisdiction and what are the tax payment dates/deadlines?

Different tax years apply to different taxpayers.

The tax year for federal income tax for individuals in the US is a calendar year. The individual's income tax return (Form 1040) is due on 15 April of the year following the end of the calendar year, although this deadline may be automatically extended for six months (that is, until 15 October), by filing Form 4868.

Likewise, an individual's tax year for federal gift tax is the calendar year. Individuals must report taxable gifts made during the calendar year in their federal gift tax return (Form 709) and pay the corresponding gift tax no later than 15 April of the year following the end of the calendar year in which the gifts were made. If the individual has extended the deadline for his income tax return (Form 1040), or has applied for an automatic six-month extension under Form 8892, the due date for filing for the gift tax return (but not for paying the gift tax) is extended until 15 October.

In general, trusts and estates are treated as separate taxpayers under US tax law and are obligated to pay tax on their income and file their own tax returns. With regards to income tax on estates, an executor can select a calendar year or any other 12-month period (called a "fiscal year") as the estate's income tax year. The estate's income tax return (Form 1041) will be due three and a half months after the close of the fiscal year and payment of any income taxes owed by the estate is due at that time. For federal income tax purposes, the tax year for trusts is the calendar year, and the deadline for filing the income tax return is 15 April of the following year. For estate tax, an executor is responsible for filing a federal estate tax return, which is due nine months after the deceased person's (decedent) death (*see Question 23*).

Domicile and Residence

2. What concepts determine tax liability in your jurisdiction (for example, domicile and residence)? In what context(s) are they relevant and how do they impact on a taxpayer?

Domicile

An individual will be domiciled in the US if they are present in the US and intend to remain in the US indefinitely.

Tax residency for federal estate and gift tax purposes is generally determined by domicile (*see below, Residence: Estate and gift tax*). By contrast, tax residence for federal income tax purposes is determined under different rules that take into account an individual's physical presence within the US (regardless of domicile) (*see below, Residence: Income tax*).

However, the US imposes its income tax, estate and gift tax on its citizens, regardless of their residence or domicile.

Residence

Resident status determines whether a person is subject to the US income and/or estate tax regimes. Residency classifications are different for income tax and federal estate and gift tax purposes.

Income Tax. The term resident generally includes someone who either:

- Holds a green card (permanent residence test).
- Spends 183 days or more in the US during the taxable year (substantial presence test).

Those who are tax resident for income tax purposes (regardless of citizenship) are taxed on their worldwide income, regardless of source. US citizens must pay US income tax regardless of residence, and the income tax applies on a global basis, regardless of where it is earned.

Non-citizens who are not resident in the US for income tax purposes are referred to as "non-resident aliens" (NRAs). NRAs are generally subject to federal income tax only on US-source income.

Estate and Gift Tax. If an individual is domiciled in the US, he or she is generally a US resident for federal gift and estate tax purposes. A US resident (or citizen) is subject to US estate tax on his/her worldwide assets on death and to US gift tax on transfers of property by gift during life. NRAs are only subject to US estate tax on property deemed located in the US on death and to US gift tax on lifetime gratuitous transfers of property located in the US (*see Question 7 and Question 8*).

Taxation on Exit

3. Does your jurisdiction impose any tax when a person leaves and/or renounces their citizenship (for example, an exit tax)? Are there any other consequences of leaving (particularly with regard to individuals domiciled in your jurisdiction)?

The following can be subject to tax under alternative tax regimes:

- US citizens who have renounced citizenship on or after 17 June 2008.
- Certain long-term US residents ("green card" holders) who have terminated resident status on or after 17 June 2008.

Only persons that meet one or more of the following thresholds will be subject to the regimes:

- Individuals with a minimum net worth of USD2 million.

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- Individuals with an average annual income of more than USD160,000 per year (taxable years beginning in 2015) for the preceding five years.
- Individuals who have failed to certify on Form 8854 that compliance has been met for all US federal tax obligations for the five years preceding the date of expatriation or termination of residency.

The regimes are contained in the following sections of the Internal Revenue Code 1986 (as amended)):

- 877A (in relation to income).
- 2801 (in relation to gifts and bequests).

Temporary Residents

4. Does your jurisdiction have any particular tax rules affecting temporary or partial year residents?

NRAs may be liable for income taxes as a US resident under the substantial presence test (*see Question 2, Residence: Income tax*). Unless the NRA satisfies this test, they will not be subject to US tax just for owning US real estate, provided the real estate is not generating income as a rental property (any rental income, however, will be subject to tax as US-source income).

Furthermore, if an NRA owns real estate located in the US at the time of his/her death, the real estate will be subject to US estate taxes (and any applicable state estate taxes) even if the he or she fails the substantial presence test (*see Question 7, Estate Tax*).

Taxes on the Gains and Income of Foreign Nationals

5. How are gains on real estate or other assets owned by a foreign national taxed? What are the relevant tax rates?

Taxation of gains on real estate or other assets owned by foreign nationals depends on the individual's residence (*see Question 2*).

If a foreign national is treated as a resident for federal income tax purposes in the relevant tax year, they will be subject to taxation on their worldwide income for that year, including gains on real estate or other assets (whether or not located in the US). However, if the foreign national is treated as an NRA for the relevant year, they will be subject to taxation on only certain discrete classes of income, including gains on real estate or other physical property located in the US.

The tax rate for gains will depend on the:

- Use of the property by the taxpayer.
- Length of time the property was held.
- Marginal tax bracket of the taxpayer.

In general, if property qualifies as a capital asset and is held for more than one year, the maximum capital gains rate is 20%. An additional 3.8% tax may apply to certain net investment income of individuals, estates and trusts that have income above the statutory threshold amounts. At the time of writing, there are several legislative proposals to raise the relevant tax rates.

In addition, the disposition of an interest in US real estate by an NRA is subject to the Foreign Investment in Real Property Tax Act of 1980 (FIRPTA) income tax withholding. The FIRPTA requires a person acquiring US real estate (or an interest in the property) from an NRA to withhold 15% of the gross amount realised on the disposition. If the purchaser fails to withhold the 15%, they may be liable for the tax. If the tax on the actual gains would be less than the 15% withholding amount, the NRA can file a federal income tax return and claim a refund.

6. How is income received by a foreign national taxed? Is there a withholding tax? What are the income tax rates?

Taxation on income received by a foreign national generally depends on residence (*see Question 2, Residence*). If the foreign national is treated as a resident for federal income tax purposes in the relevant tax year, they will be subject to taxation on their worldwide income for that year. However, if the foreign national is treated as an NRA for the relevant year, they will be subject to taxation on only certain discrete classes of income including:

- Wages for services performed in the US.
- Gains on the sale of real estate and other physical property located in the US.
- Dividends, interest and other income from certain US sources.

The income tax rate depends on the class of income received and the taxpayer's marginal income tax rate:

- Wages and other ordinary income are generally subject to progressive tax rates (under present US law, the highest tax rate for 2021 is 37% for individuals earning over USD523,600 for unmarried individuals and USD628,300 for married couples filing a joint return).
- Qualified dividends and long-term capital gains are generally subject to tax at the maximum rate of 20%.
- An additional 3.8% tax may apply to certain net investment income of individuals.
- Estates and trusts that have income above the statutory threshold amounts.

At the time of writing, there are several legislative proposals to raise the relevant tax rates.

Perhaps most relevant for foreign nationals are dividends, interest and other fixed, determinable, annual or periodic income from US sources (FDAP income). FDAP income is subject to withholding at the source of payment. Payors of FDAP income (generally banks and investment brokers) to certain non-US persons must withhold 30% of the gross amount of such payments. However, in practice, the statutory withholding rate is reduced (often to 0%) for residents of certain non-US jurisdictions that have an income tax treaty is effect with the US. All or a portion of the withholding amount on FDAP income may be refunded if the NRA files a federal income tax return and claims a refund. However, many NRAs who otherwise have no income tax payment or filing obligations in the US often choose not to do so.

Tax at Death

7. What taxes are imposed on the death of an individual? What is the basis of the inheritance tax or gift tax regime (or alternative regime if relevant)?

Estate Tax

In general, the US imposes an "estate tax" on the estates of decedents rather than an "inheritance tax" on the inheritance received by heirs. Federal estate tax is calculated based on the fair market value of the assets owned by the decedent at death (or deemed to be owned by the decedent under the relevant tax rules), net of any debts and applicable deductions and exclusions, and is payable by the decedent's estate.

For decedents dying in 2016 (before the enactment of the Tax Cuts and Jobs Act 2017 (TCJA)), the federal estate tax rate was 40%, with a USD5.45 million applicable exclusion amount (*see Question 8, Tax Free Allowance*), or a USD60,000 applicable exclusion

amount for NRAs. However, the enactment of the TCJA has doubled the applicable exclusion amount, indexed for inflation.

For decedents dying in 2021, the maximum federal estate tax rate remains 40%, with a USD11.7 million applicable exclusion (USD60,000 for NRAs). Unless the federal government takes additional action, many of the relevant provisions of the TCJA will "sunset" on 1 January 2026, including the automatic reduction of the applicable exclusion amount to its previous, lower value (but indexed for inflation through 2026).

The application of the estate tax will depend on whether or the individual is:

- **A US citizen/resident.** Estate tax is charged on the fair market value (FMV) of all assets owned by the decedent at death (or deemed to be owned by the decedent under the relevant tax rules), net of any debts and applicable deductions and exclusions. All such assets, regardless of location in the US or abroad, are generally subject to such tax.
- **An NRA.** Estate tax is charged on the FMV of all assets owned by the decedent at death (or deemed to be owned by the decedent under the relevant tax rules) and that are deemed to be located in the US. Assets deemed to be "located" in the US would include US real estate, tangible personal property located in the US, as well as shares of stock of a US corporation (regardless of where the stock certificates are held). Relevant debts and other applicable deductions and exclusions may reduce the net value of the assets subject to federal estate tax. In addition, many countries have estate tax treaties with the US which provide exceptions, exclusions and other benefits to residents of the treaty countries (*see Question 13*).

Gift Tax

Gift tax is calculated at the time of the gift and on the FMV of the gifted assets. A US citizen or resident is taxed on gifts made on a worldwide basis. NRAs are generally only subject to gift tax on gratuitous transfers of tangible property and real estate situated in the US.

Although the gift tax rules for NRAs are similar to the relevant estate rules, treatment of intangible property represents an important exception. Federal estate tax applies to shares in a US company owned by the NRA decedent. However, lifetime gifts of such shares by NRAs are not generally subject to federal gift tax. The gift tax is payable by the donor no later than 15 April of the year following the year the gift was made (even if the taxpayer has extended the deadline for filing the gift tax return).

Generation-skipping Transfer Tax (GST)

In addition to estate and gift tax, the federal tax system imposes another wealth transfer tax called the "generation-skipping transfer" tax (GST Tax).

This applies to transfers of property (whether at death or during life) to persons of two or more generations below the transferor (such as a grandchild or great-grandchild). GST tax is imposed in addition to any estate or gift tax that would also apply to the transfer. Unlike federal estate or gift tax, GST tax also applies to trusts (for example, when trust distributions are made to the grantor's grandchildren (or more remote descendants) or when the beneficial interest in the trust passes to the grantor's grandchildren (or more remote descendants)).

Transfers by NRAs are generally not subject to the GST tax.

Inheritance Tax on Covered Gifts and Bequests

"Covered expatriates" are subject to an alternate wealth transfer tax regime under US law. Such persons include certain former citizens and long-term residents of the US who renounced their citizenship and/or terminated residency status and have exceeded the statutory net worth or income levels.

Covered expatriates are treated similarly to NRAs for federal estate and gift tax purposes. For example, federal estate and gift tax would generally only apply to transfers of property located in the US. However, US citizens and residents must report receipt of certain transfers of property received from covered expatriates (called "covered gifts and bequests"). Under US tax law, covered gifts and bequests include property acquired directly or indirectly by gift from a covered expatriate or by reason of the death of the covered expatriate. The recipient (rather than the covered expatriate or his/her estate) must pay US inheritance tax on the FMV of the covered gift or bequest, which is computed based on the highest estate tax rate then in effect.

8. What are the rates of tax for each type of tax levied at death?

Tax Rates

Estate and gift tax rates are imposed on a unified rate structure, which means that the marginal rates of tax are the same for estate and gift tax.

Under the American Taxpayer Relief Act 2012 (ATRA), the maximum federal estate and gift tax rates were set at 40%. This tax rate presently remains in place under the TCJA.

Gift tax is generally more efficient for the taxpayer than estate tax. This is because gift tax is imposed on a "tax-exclusive" or net basis, whereas estate tax is imposed on a "tax-inclusive" or gross basis. This means that:

- Estate tax is imposed based on the FMV of the assets owned by the taxpayer at the time of death (net of debts and other applicable deductions or exclusions), including the funds that will be remitted to the US government in payment of the estate tax.
- Gift tax is imposed on the net value of the gift transferred and the donor (rather than the donee) is obligated to pay the tax.

In addition to the federal gift and estate taxes, the maximum rate for GST tax is also set at 40%.

Tax Free Allowance

Applicable Exclusion Amount. US citizens and residents are entitled to an exemption from federal estate and gift taxes known as the "applicable exclusion amount".

Under the ATRA (before the enactment of the TCJA) the applicable exclusion amount was USD5.45 million for 2016. However, the TCJA has doubled the applicable exclusion amount to USD11.7 million (as indexed for inflation) for 2021. Subject to any further changes introduced by the federal government, many of the relevant provisions of the TCJA will "sunset" as of 1 January 2026, which will involve the automatic reduction of the applicable exclusion amount to its previous, lower levels (but indexed for inflation through to 2026).

Under the "unified" federal estate and gift tax system, the applicable exclusion amount functions as a cumulative tax-free allowance for US citizens and residents for taxable gifts during life and/or the individual's taxable estate at death. Lifetime gifts will automatically reduce the individual's applicable exclusion amount so that gift tax will not become payable unless and until an individual's cumulative taxable gifts exceed the applicable exclusion amount. If the individual does not "use" all of his applicable exclusion amount by making lifetime gifts, the remaining balance will shield a portion of his taxable estate at death (and only the net value of his taxable estate will be subject to estate tax).

Since each US citizen and resident is entitled to his or her own applicable exclusion amount and that transfers between US citizen spouses do not attract federal gift or estate tax. Married couples

can use intelligent planning to maximize the benefit of both spouses' applicable exclusion amounts.

A typical structure is for married couples to create a trust on the death of the first spouse, which can be funded with assets equal to the value of the deceased spouse's remaining applicable exclusion amount. The deceased spouse's applicable exclusion amount can be applied to that trust and (assuming the balance of the deceased spouse's estate passes to the benefit of the surviving spouse) no federal estate tax may therefore be payable on the first spouse's death, regardless of the size of the estate. On the death of the surviving spouse, the amounts in the credit trust can then be distributed to further trusts for the benefit of children or other descendants without attracting any federal estate tax on the surviving spouse's death.

The ATRA has also confirmed "portability" of the applicable exclusion amount between spouses. Portability allows the surviving spouse to use the portion of the deceased spouse's unused applicable exclusion amount (which would be in addition to the surviving spouse's separate applicable exclusion amount), therefore increasing the effective tax-free allowance available to the surviving spouse. In the case of multiple marriages, portability is limited to only the most recently deceased spouse. The deceased spouse's executor must affirmatively elect portability on a timely filed federal estate tax return. Portability does not apply for GST tax purposes.

Annual Exclusion. In addition to and separate from the applicable exclusion amount, US citizens and residents can also exclude the first USD16,000 of gifts made each year per each recipient. This tax-free gift amount is called the "annual exclusion". There is no limit to the number of annual exclusions that each donor can make each year and the amount of the annual exclusion is indexed for inflation (in USD1,000 increments). For example, a donor can give USD16,000 to each of his children, grandchildren and any number of other recipients without paying gift tax and without reducing his applicable exclusion amount. Gifts to trusts do not qualify for the annual exclusion unless the beneficiaries of the trust have the power to withdraw the gift. Although the amount of the annual exclusion is small, great savings can be achieved over time.

Unlimited Exclusion for Medical and Education Payments. Payments for certain qualified educational and medical expenses are also excluded from the US gift tax.

Transfers to Non-Citizen Spouses. Transfers to a spouse who is US citizen and to qualified charitable organizations are fully deductible for purposes of federal estate and gift tax. Outright transfers to a non-citizen spouse, however, that exceed the annual limit (USD164,000 for 2022 and adjusted annually for inflation), will be subject to gift tax.

Techniques to Reduce Liability

US citizens and residents often employ the following techniques to manage and reduce tax liability:

- **Lifetime gifts.** US citizens and residents can make gifts up to the lifetime applicable exclusion amount without incurring federal gift tax (*see above, Tax Free Allowance*). Gifted property will not be included in the donor's estate upon his future death and thus will not be subject to estate tax at that time. Since future income and appreciation on the gifted property also escape estate tax, lifetime gifts provide an attractive opportunity to manage and reduce future tax liability.

- **Trusts.** Trusts can be very powerful tax and estate planning tools. Trusts are not subject to federal estate or gift taxes, so trusts are typically preferred as the recipient of lifetime gifts (compared to outright gifts to beneficiaries since assets owned by an individual will become subject to estate tax on the individual's death). Furthermore, a trust that is exempt from GST tax can continue for the term of the trust without its assets ever becoming subject to federal wealth transfer taxes. Many US jurisdictions have abolished a common law rule (the "rule against perpetuities") that limited the maximum lifespan of a trust and have explicitly authorised perpetual trusts. US estate planners have also developed several specific tax-efficient strategies involving trusts, which include the following:

  - a grantor-retained annuity trust (GRAT);
  - a sale of assets to a grantor trust;
  - a qualified personal residence trust (QPRT); or
  - a charitable trust, such as a charitable lead annuity trust (CLAT), charitable lead unitrust (CLUT), or charitable remainder unitrust (CRUT) or annuity trust (CRAT).

- **Limited liability companies (LLCs) and limited partnerships (LPs).** These are generally treated as invisible for US income tax purposes (unless an affirmative election is made to be taxed as a corporation) and therefore there is only one level of income tax. The owners (and not the LLC or LP itself) pay income tax on their share of the entity's income as that income is realised, and no tax is generally payable when the owners receive dividends or distributions from the entity. LLCs and LPs also have the advantage of limited liability for their owners from any creditor claims against the entity or other owners. LLCs and LPs are attractive vehicles not only for holding and managing assets, but also for tax-wise estate planning. For example, LLC or LP owners can make gifts of shares or other ownership interests in the LLC or LP directly to younger generations (or to a trust for their benefit). For federal gift tax purposes, the FMV of the transferred interests may reflect a "discount" to the underlying value of the assets held in the LLC or LP, which reflect the lack of control and lack of marketability for this interest. Therefore, in certain situations a greater "real world" value can be shifted from the transferor to the transferee at a lower value for gift tax purposes.

9. Does the inheritance tax or gift tax regime apply to foreign owners of real estate and other assets?

The US imposes federal gift and estate tax on transfers of certain assets by NRAs. Federal gift tax applies to gifts from NRAs of real estate and other physical property situated within the US. Gifts of intangible property by NRAs (including gifts of shares in US corporations) are not generally subject to federal gift tax, regardless of whether the gift was made to a US citizen/resident or US trust.

Federal estate tax applies to the estate of a NRAs to the extent of any interest in the following property:

- Real estate situated in the US.
- Other physical property located in the US at the time of the NRA's death.
- Shares in US corporations.
- Other property deemed to have a US situs under the federal tax rules.

Transfers by NRAs of certain intangible property (such as shares in US corporations) are not subject to federal gift tax, but would be subject to federal estate tax if owned by the NRA at the time of his/her death.

NRAs are not entitled to the applicable exclusion amount allowed for US citizens and residents (USD12.06 million for 2022 and indexed annually for inflation) (*see Question 8, Tax Free Allowance: Annual Exclusion*). Instead, NRAs receive a much lower exclusion of USD60,000 (not indexed for inflation).

The gift and estate tax rates for NRAs are the same as those for residents (*see Question 8, Tax Rates*).

10. Are there any other taxes on death or on lifetime gifts?

In addition to the federal estate, gift and GST taxes, US citizens and residents can also be subject to wealth transfer taxes imposed by local jurisdictions. The US includes more than 50 state or other local jurisdictions that share taxing authority with the federal government. Many of these jurisdictions impose estate or inheritance taxes that apply both to the residents and to non-residents who own property located in the state. At writing, only one jurisdiction (Connecticut) imposes a gift tax on lifetime gifts as well.

If a US citizen or resident makes a lifetime gift of appreciated property to a foreign trust or estate, an exit tax may be charged on the unrealised gains. No tax is charged on outright gifts to NRAs or on testamentary transfers to foreign trusts or estates.

Taxes on Buying Real Estate and Other Assets

11. Are there any other taxes that a foreign national must consider when buying real estate and other assets in your jurisdiction?

Purchase and Gift Taxes

Taxes are imposed by the Foreign Investment in Real Property Tax Act of 1980 (FIRPTA). If a foreign individual or entity sells US real estate (including, for this purpose, a share of private condominium (that is, a building or complex containing a number of individually owned flats or houses) or co-operative apartment) for gain, the buyer may be required to withhold 15% of the purchase price to ensure the US receives any applicable taxes on the gain.

Local taxes, such as transfer taxes, can be imposed on either the purchaser or seller of real estate. These can include:

- A "flip tax", which condominium associations and co-operative apartment associations often impose on either the buyer or seller, sometimes at the time of purchase. (Although not technically a "tax" since it is not imposed by a government authority, the flip tax is still a material financial consideration for purchasers and sellers). Flip taxes are common in New York City co-operative apartments.
- A surtax where expensive real estate is purchased and sold. This tax (called a "mansion tax" in New York) is imposed by certain states or cities, frequently when the value of the property exceeds a certain threshold (such as around USD1 million).
- Taxes whose application depends on the relationship between the purchaser and seller. Often, they do not apply when these parties are related.

Conveyance taxes may be imposed at the state or local level when title is transferred.

VAT

There is no federal VAT on goods or services in the US. Instead, nearly all US states impose state-wide sales taxes. The US territory of Puerto Rico was briefly set to impose a VAT in lieu of its sales tax in 2016, but the territory's legislature voted to repeal it prior to implementation.

Wealth Taxes

See *Question 7* and *Question 8*.

Property Taxes

In the US, state and other local jurisdictions levy annual taxes on real estate and, in some cases, other property located in the relevant jurisdictions. Real estate taxes are generally based on the value of the property, which is adjusted periodically, for example, when the property is sold and pursuant to jurisdiction-wide reassessments.

12. What tax-advantageous real estate holding structures are available in your jurisdiction for non-resident individuals?

LLCs and LPs are common and attractive structures for holding assets, and are particularly favoured for real estate holdings (*see Question 8, Techniques to Reduce Liability*).

NRAs face different tax attributes than citizens and residents. In particular, NRAs are subject to federal estate tax on US real estate owned directly or through wholly owned LLCs and LPs as well as shares in a US corporation. For that reason, many NRAs often hold their US real estate through more complex structures to avoid or limit their exposure to US estate tax (for example, through shares in non-US corporations, which are not subject to federal real estate tax).

An alternative option is for the NRAs to purchase their US real estate through an irrevocable trust, which would not be subject to estate tax on the NRA's death. A non-US trust would not be subject to FIRPTA withholding when the underlying US real estate is sold, although a US trust would not be subject to FIRPTA withholding. If the NRA originally purchased the US real estate through another structure, federal gift tax could apply upon a transfer of the US real estate to an irrevocable trust.

Taxes on Overseas Real Estate and Other Assets

13. How are residents in your jurisdiction taxed on real estate or other assets owned outside of the jurisdiction?

US residents and citizens are taxed on their worldwide income, regardless of source, including:

- Interest and dividends derived from sources outside the US.
- Rentals or royalties from property located outside the US, or from any interest in such property.
- Gains, profits, and income from the sale or exchange of real property located outside the US.

Similarly, US residents and citizens are subject to US wealth transfer taxes on lifetime or testamentary transfers of assets wherever located. For example, lifetime gifts of foreign real estate by US citizens or residents will be subject to federal gift tax and testamentary transfers of foreign real estate by US citizens or residents will generally be subject to federal estate tax. GST tax may apply to either of those transfers if and when the benefits of the transferred property pass for the benefit of individuals that are two or more generations below the transferor (*see Question 7, Generation-skipping Transfer Tax (GST)*).

International Tax Treaties

14. Is your jurisdiction a party to many tax treaties with other jurisdictions?

The US has an extensive network of tax treaties with many jurisdictions (including the UK). These treaties generally ensure that the tax regimes of the contracting countries are respected. They usually provide that the citizens or residents of either or both of the contracting countries are liable for tax at the higher rates of the two countries, with the country in which the citizen or resident resides being entitled to the bulk of the tax. A contracting country is generally entitled to tax real estate located in that country or a

trade or business conducted in that country. The treaty determines numerous other aspects of the taxing regimes.

The US has not enacted general anti-avoidance rules (GAARs). However, most US-bilateral tax treaties do include various specific anti-avoidance rules (SAARS), including:

- Beneficial ownership requirements.
- Limitation on benefits (LOB) provisions.
- Limitation on residents' provisions.

The US has also enacted, by domestic legislation, various SAARS, including the reporting rules under the Foreign Account Tax Compliance Act (FATCA). Under FATCA, certain US taxpayers holding financial assets outside the US must report those assets to the IRS on Form 8938, Statement of Specified Foreign Financial Assets (this requirement is in addition to the long-standing requirement to report foreign financial accounts on FinCEN Form 114, Report of Foreign Bank and Financial Accounts (FBAR)). The requirements imposed by FATCA are outside of the scope of this Q&A.

Automatic Exchange of Tax Information

15. Has your jurisdiction implemented the Organisation for Economic Co-operation and Development's (OECD's) multilateral Common Reporting Standard (CRS) into its domestic law?

The US is not a participating jurisdiction to the OECD's CRS.

WILLS AND ESTATE ADMINISTRATION

Governing Law and Formalities

16. Is it essential for an owner of assets in your jurisdiction to make a will in your jurisdiction? Does the will have to be governed by the laws of your jurisdiction?

In the US, the rules regarding the validity, application and interpretation of wills are determined according to state law rather than federal law.

In general, US states recognise the validity of a will that complies with the formalities and other requirements of the jurisdiction in which the will was executed and/or the jurisdiction of the testator's domicile (either at the time of the will's execution or the time of testator's death).

If the will is to be made by an NRA, it is best practice to ensure that the NRA's will complies with the applicable formalities and other requirements of the state in which the property is located. In many circumstances, it may be desirable to have a separate will that applies only to the property located in the US (for example, where the individual's domicile is not English-speaking or if his/her primary testamentary instruments would need to be translated). Although a non-English will is acceptable for probate in state courts (along with a certified translation), the probate process and administration would likely be more expeditious and efficient if the will is in a form more recognisable and familiar to court personnel.

17. What are the formalities for making a will in your jurisdiction? Do they vary depending on the nationality, residence and/or domicile of the testator?

The formalities and other requirements for making a will in the US are determined according to state law. Although each state prescribes its own rules by statute, many states require the testator to subscribe the will in the presence of at least two disinterested witnesses. Wills can also be "self-proved" by the testator and attesting witnesses by including an additional clause or affidavit at the end of the will that is sworn to or acknowledged before a notary public. A "self-proved" will allows for a more expedited probate process.

Despite the patchwork of state-by-state requirements, US jurisdictions also generally recognise the validity of wills executed in compliance with the formalities of other jurisdictions (including not only other US states but also foreign jurisdictions as well). For example, a state may validate a will executed in compliance with the formalities of the following jurisdictions (in addition to its own rules):

- The jurisdiction of the testator's domicile (either at the time the will was executed or the time of the testator's death, or both).
- The jurisdiction where the will was executed.
- With respect to particular real property, business assets or other physical property, the jurisdiction where such property is located.

Nevertheless, the best practice is to ensure that the testator's will (or other testamentary instrument) complies with the formalities and other requirements of the state or other jurisdiction where the property is located.

Electronic Wills

18. Is it possible for a will to be made electronically? What are the formalities for making and executing an electronic will remotely?

Several US states (including Nevada and Florida) have enacted statutes that allow for electronic wills and/or the electronic execution of wills and other testamentary instruments. In addition, several states (including New York) approved temporary procedures for "remote" execution/witnessing of wills and other instruments during the COVID-19 pandemic.

At present, practitioners have not yet accrued sufficient experience with these innovative practices and techniques, in particular with respect to the probate and administration process for a decedent's estate. The best practice is therefore to favour the well-established, "manual" techniques for executing wills and other testamentary documents, although these novel alternatives should be considered if it is not otherwise possible for the client to execute a will under the traditional method.

Redirecting Entitlements

19. What rules apply if beneficiaries redirect their entitlements?

Under US law, individuals can "disclaim" or "renounce" their interest in an estate, trust or other gratuitous transfer of property.

State property law sets the requirements for an effective disclaimer or renunciation and also determines the alternative recipient of the disclaimed property. The requirements for an effective disclaimer or renunciation vary by state but often require a written (and, possibly, notarised) statement by the disclaimant, notice to the executor or trustee and, potentially, a court filing. In general, state law treats the disclaimant as having predeceased the testator/transferor and thus the will or other relevant instrument would be interpreted and applied accordingly.

Validity of Foreign Wills and Foreign Grants of Probate

20. To what extent are wills made in another jurisdiction recognised as valid/enforced in your jurisdiction? Does your jurisdiction recognise a foreign grant of probate (or its equivalent) or are further formalities required?

State law determines the extent to which foreign wills will be given effect (*see Question 16*).

In the case of real estate, the foreign will must generally be executed in compliance with the formalities and other requirements of the jurisdiction where the property is located.

In the case of personal property, the foreign will must generally be executed in compliance with the formalities and other requirements of the jurisdiction where the testator was domiciled at the time the will was executed or at the time of his death.

In general, a foreign will would not be offered for probate in a US state unless the testator owned real estate or other property physically located in the state or the testator became domiciled in that state after executing the foreign will (and did not subsequently execute a new will in accordance with the rules of his new domicile).

Subject to certain exceptions, US states will generally recognise the validity of a foreign will admitted to probate in a foreign jurisdiction. However, even when a valid will is admitted to probate in a foreign jurisdiction, state law will often require a separate "ancillary" probate proceeding in state court to administer and transfer any real property owned by the decedent and located in the state.

Death of Foreign Nationals

21. Are there any relevant practical estate administration issues if foreign nationals die in your jurisdiction?

Unless a foreign national was a resident of (that is, domiciled in) the US at the time of his/her death, it is unlikely that his/her will would be admitted to probate in the US or that his/her estate would be administered in the US. If the foreign national owned property located in the US, the disposition of that property would be governed by the law of the state where the property was located and the validity of his/her will with respect to that property would be determined under that state's law.

The location of an individual's death has no particular relevance to the administration of his or her estate. However, the location and circumstances of an individual's death may be relevant to the issuance of a death certificate and other vital records that will be important for probate and other issues relating to succession and estate administration.

Administering the Estate

22. Who is responsible for administering the estate and in whom does it initially vest?

Responsibility for Administering

The role and power of executors (also called "personal representatives" in some states) is determined according to state law. The beneficiaries hold the beneficial interest in the estate, although the executor usually holds legal title during administration.

The duties of the executor include:

- Identifying, marshalling and valuing the assets of the decedent.
- Preparing and filing estate, income and other required tax returns and paying federal and state estate, income and other required taxes.
- Paying the valid debts and other expenses of the decedent.
- Transferring the decedent's assets according to the terms of the will.

Vesting

Vesting is determined according to state law. Generally, specific bequests vest in a beneficiary as of the date of death and other property vests at the time of distribution. The traditional rule of the common law, still followed with modifications in some states, is that real estate vests automatically in the beneficiaries (whether or not such property is specifically devised).

23. What is the procedure on death in your jurisdiction for tax and other purposes in relation to establishing title and gathering in assets (including any particular considerations for non-resident executors), paying the necessary taxes and distributing the estate?

Establishing Title and Gathering in Assets

In the US, most property questions are determined under state law. Any assets owned in the individual name of a decedent generally become a part of his "probate estate" administered pursuant to the state law of succession. If a will is offered for and admitted to probate, the court appoints an executor who has the responsibility for marshalling, administering and distributing the decedent's assets and otherwise carrying out the terms of the will. If the decedent does not have a will (that is, dies "intestate"), the court appoints an administrator who becomes responsible for administering the probate estate and ultimately transferring the decedent's assets pursuant to the state statute of descent and distribution.

If the decedent owned any assets in his/her capacity as trustee (for example, if the decedent was the trustee of a revocable trust), a successor trustee will be appointed pursuant to the terms of the trust instrument. Court involvement is not typically necessary unless there are unusual circumstances (for example, where there is a unprovided-for vacancy in the trusteeship). The successor trustee then becomes responsible for administering the trust property in accordance with the terms of trust instrument.

In the US, many decedents have valuable rights in "non-probate" assets (such as retirement accounts, life insurance policies, jointly owned real estate and financial accounts with a "pay on death" or "transfer on death" feature). In general, these assets do not form a part of the decedent's probate estate, are not subject to administration by the executor and are not subject to disposition under the terms of the decedent's will. Rather, the disposition of these assets are governed by contractual terms, which may include a beneficiary designation on file with the financial institution in the case of insurance policies, retirement accounts and other financial accounts.

The decedent's debts and expenses are usually charged to his/her probate estate (rather than non-probate assets). However, the allocation of the burden for paying estate taxes can be determined by the decedent's will (or in the absence of a specific provision, by state statute).

Procedure for Paying Taxes

The federal estate tax return, along with payment for any estate tax liability, is due nine months after the decedent's death. The deadline for filing the return (although not for paying the tax liability) may be extended automatically for six months without a showing of cause (that is, providing reasons). An extension for

paying the tax liability, along with additional extensions for filing the return, may be available on a showing of cause.

In addition, the estate tax liability associated with certain types of assets may be deferred over an extended period of time. Most notably, in certain circumstances, the estate tax associated with an interest in a family-owned business may be deferred for five years and then paid in equal instalments over an additional ten-year period (section 6166, Code). During the five-year deferral period, the estate is only required to make interest payments at the prescribed rate. To qualify for this deferral, generally more than 35% of the adjusted gross estate of the decedent must consist of eligible interests in a family-owned business.

The IRS may audit the estate tax return any time within three years of the date when the estate tax return is filed (absent fraud or other extraordinary circumstances). In the course of an audit, the IRS may adjust the value of estate assets, reduce the amount of any deductions or otherwise assess a higher tax than reported on the return.

To secure the payment of estate tax, the Code automatically imposes a lien on all of the decedent's property. The executor may therefore need to obtain a waiver of lien from the IRS before disposing of the property (for example, prior to selling real estate).

For federal income tax purposes, an estate (like a trust) is treated as a separate taxpayer. The estate of a US citizen or resident has similar obligations as a citizen or resident individual with respect to paying federal income tax and filing income tax returns, whereas the estate of an NRA (a "foreign estate") is similar to a non-citizen/non-resident individual in those respects (*see Question 32, Tax Laws: Type of Trust and Taxation*). However, estates do not need to make estimated income tax payments during the first two years following the death of the decedent.

Distributing the Estate

In general, before distributing the assets to the beneficiaries, the executor should ensure that all estate obligations have been satisfied, including:

- Payment of all federal and state estate taxes.
- Payment of the decedent's enforceable debts and other expenses.

An executor customarily also obtains from the beneficiaries an agreement to refund the estate for any additional taxes, expenses or other obligations and indemnify the executor against any personal liability for those payments. (Under the federal and state law, the executor could be personally liable for failure to pay estate taxes.) The best practice is for the executor nevertheless to retain a reserve for payment of additional taxes and expenses until receipt of a closing letter from the IRS or the final settlement of the estate's tax obligations.

24. Are there any time limits/restrictions/valuation issues that are particularly relevant to an estate with an element in another jurisdiction?

Foreign estates are generally subject to the same processes and procedures, including tax payment and filing deadlines, as the estates of citizens and residents (*see Question 21*).

25. Is it possible for a beneficiary to challenge a will/the executors/the administrators?

With limited exceptions, US law recognises a broad right to testamentary freedom. Children, for example, generally have no right to an inheritance from their parents and therefore cannot challenge a will for the mere fact that they have been excluded.

One notable exception to this policy are spousal rights. Some US states, for example, follow the common law system of separate property for married couples, with a surviving spouse usually entitled to elect to receive a minimum percentage of a decedent's estate (regardless of what the will specifically provides).

Nevertheless, a decedent's heirs may challenge the validity of the will on other grounds as determined under state law. For example, virtually all states permit challenges to a will, trust and other gratuitous transfers for noncompliance with the required formalities, lack of testamentary capacity, undue influence, fraud or duress.

Wills and other instruments often contain "in terrorem" clauses that automatically forfeit a beneficiary's interest if that beneficiary initiates or supports a challenge. However, state law will determine whether, and the extent to which, these clauses will be enforceable.

SUCCESSION REGIMES

26. What is the succession regime in your jurisdiction (for example, is there a forced heirship regime)?

Succession regimes vary according to state law. Forced heirship for children generally does not exist in the US. However, many states provide minimum shares of the estate for surviving spouses.

Forced Heirship Regimes

27. What are the main characteristics of the forced heirship regime, if any, in your jurisdiction?

There is no federal forced heirship regime in the US. However, the State of Louisiana has rules that provide for forced heirship in certain circumstances and the laws of the State of Florida also have certain restrictions on transfers at death which may be considered a form of forced heirship. Under this rule, a home in Florida owned and occupied by a decedent (called a "homestead") cannot be freely transferred at death by the decedent if the decedent is survived by a spouse or a minor child or minor children (*section 732.4015, Florida Statutes*). However, the homestead can be transferred to the decedent's spouse if there are no minor children.

States' courts may nevertheless, in some cases, apply the law of another jurisdiction to an estate administered in the US, which may include the forced heirship regime or other laws affecting a beneficiaries' rights in the estate.

Real Estate or Other Assets Owned by Foreign Nationals

28. Are real estate or other assets owned by a foreign national subject to your succession laws or the laws of the foreign national's original country?

Real estate located in the US is subject to the succession laws of the state where it is located. State law also determines the validity of the will with regard to any real estate located within that particular state. By contrast, states generally apply the law of the decedent's last domicile for questions of succession relating to personal property.

If a foreign national is domiciled in the US, then the succession law in the state of domicile will generally apply to their estate (except with respect to real estate located elsewhere). The restrictions on the decedent's testamentary freedom would in that case be the same as a US citizen that was domiciled in the state.

29. Do your courts apply the doctrine of *renvoi* in relation to succession to immovable property?

In the US, choice of law rules are determined under state law that have historically been developed through individual court decisions. The strong tendency of US courts has been to reject the doctrine of *renvoi*. Rather, when applying the law of another jurisdiction, state courts generally look only to the substantive law of that other jurisdiction (rather than the "whole law" which includes the choice of law rules of the other jurisdiction).

INTESTACY

30. What different succession rules, if any, apply to the intestate?

Probate and estate administration procedures are determined by state law.

In general, state law provides for the appointment of an "administrator" to fill a role analogous to the executor with respect to the probate estate of the intestate. The disposition of an intestate's probate estate is governed by the state statutes of descent and distribution. Under most states' laws, a surviving spouse and the decedent's issue become the heirs, followed by the decedent's parents, then siblings and their descendants, then grandparents, aunt/uncles and cousins. In the absence of any sufficiently close surviving kin, an intestate's property escheats to the state.

31. Is it possible for beneficiaries to challenge the adequacy of their provision under the intestacy rules?

State statutes of descent and distribution are mandatory rules for the disposition of an intestate's probate estate based on the relationship between the distributees/heirs. Therefore, an intestate's distributees or heirs cannot challenge the adequacy or fairness of these rules based on the particular circumstances.

In the case of purported parentage or kinship, or the termination or nullity of a marriage, state law generally provides a procedure for establishing or challenging such relationships.

TRUSTS

32. Are trusts (or an alternative structure) recognised in your jurisdiction?

Recognition of Trusts

The validity of trusts is determined by state law. All states but one (Louisiana) have received the English common law as it relates to trusts (as modified by later statute or specific court decision); Louisiana has recognised trusts by statute.

The rules for creating a valid trust vary by jurisdiction. Some states, such as New York, require signed and/or notarised instruments, whereas many other states will purportedly recognise oral trusts of personal property. The settlor of a trust has wide discretion to select the governing jurisdiction provided there are sufficient contacts between the relevant parties with the selected jurisdiction.

Tax Laws

Type of trust and taxation. Trusts, like estates, are treated as separate taxpayers and may have obligations to pay tax and to file tax returns.

The tax treatment of a trust depends on whether it is classified as a:

- **Grantor trust.** In a grantor trust, all items of income of the trust are taxable to the trust's grantor (whether or not income is distributed or retained within the trust for the beneficiaries). This is true even if the income may not be distributed to the grantor. The income of a grantor trust is taxed on the grantor's personal income tax return.
- A grantor trust is not generally required to file its own separate income tax return (Form 1041), although the trustee has the option to do so.
- A grantor trust can be useful for estate and tax planning purposes under US law. The grantor can make a completed gift to a grantor trust that is excluded from the grantor's estate for estate tax purposes and, during the grantor's lifetime, is required to pay the income taxes attributable to the income of the trust, thereby reducing the value of the grantor's estate and allowing the assets of the trust to appreciate for its beneficiaries as if the assets were in a tax-free environment.
- Certain specific provisions contained in the trust's governing instrument will result in the trust being treated as a grantor trust, such as:
  - the grantor's power to revoke the trust;
  - the power of the grantor (or a person who is considered "related" or "subordinate" to the grantor for US income tax purposes) to determine the beneficial enjoyment of the trust's income or corpus;
  - the grantor's power, exercisable in a non-fiduciary capacity, to substitute property of an equivalent value; or
  - the trustee having discretion to apply trust income to the payment of premiums on policies of insurance on the life of the grantor or the grantor's spouse.
- **Non-grantor trust.** Non-grantor trusts report income (both ordinary income and capital gains) for federal income tax purposes on Form 1041 and must separately report that income for state income tax on the relevant states' income tax forms.
- If a non-grantor trust makes distributions during any tax year, the trust may receive an income tax deduction for all or a portion of such distribution to the extent of the trust's "distributable net income" (DNI). The beneficiary who receives a trust distribution will generally treat all or a portion of his/her share of the trust's DNI as taxable income, and will be required to report that income on his personal income tax return and pay any associated taxes. The rules governing the computation of DNI can be highly technical, but the general purpose is to allocate income (and the associated tax) between the trust itself and the beneficiaries receiving a distribution. In effect, the trust will only pay income tax on accumulated income (that is, income that is not distributed (or deemed distributed) to beneficiaries). Capital gains are usually not included in DNI and therefore a non-grantor trust will include capital gains as a part of the trust's taxable income and pay the associated income tax regardless of distributions to beneficiaries in the relevant tax year.

Trusts classified as a "foreign trust" for federal income tax purposes will generally not be subject to income tax payment and reporting obligations (except in situations where an NRA would have analogous US tax obligations, such as in relation to income effectively connected to a US trade or business). The federal tax law defines "foreign trust" as any trust that does not meet both of the following conditions:

- A court within the US being able to exercise primary supervision over the administration of the trust.

- One or more US persons having the authority to control all substantial decisions of the trust.

(*Sections 7701(a)(30)(E) and 7701(31)(B), Code.*)

Therefore, a trust can be a foreign trust even if:

- The trust settlor is a US resident.
- All of the trust's assets are located within the US.
- All of the trust's beneficiaries are US persons.

Although foreign trusts do not generally pay federal income tax on their accumulated income, distributions to a US citizen or resident from a foreign trust are treated similarly to distributions from a US trust (to the extent of the recipient's share of the trust's DNI). In addition, if the foreign trust has accumulated income in prior years, distributions in excess of DNI are treated as distributions of the trust's "undistributed net income" (UNI). Distributions of UNI to US citizens or residents are subject to punitive taxation under the complex "throwback rules" which are beyond the scope of this Q&A. Qualified counsel should be consulted in administering a foreign trust with US beneficiaries.

Residence of Trusts. US federal income tax law does not recognise the concept of a trust's "residence" for any relevant purpose. As noted above, for federal purposes, trusts are considered foreign or not based on the court exercising primary jurisdiction and the residence of the trustees. Nevertheless, the "residence" of a trust can be crucial for state trust law and state income taxation. Whether a trust is resident in a particular state depends on the laws of the relevant state. State law may have certain rules to determine whether its trust laws apply to the trust (for example, the laws governing the trust's validity or administration), and may have other rules to determine whether the trust's income is subject to the state's income tax. These rules, which generally require sufficient contacts with a certain state, may include:

- The residence of the trust settlor at the time of the trust's creation.
- The residence of the trustee, that is:
  - the residence of the individual trustee; or
  - the state of incorporation of the corporate trustee (i.e., the bank or trust company).
- The residence of the trust beneficiaries.
- The location of some or all of the trust assets.
- The place of primary administration.

It is possible for a trust to not be deemed a resident of any state for income tax purposes or to be subject to income tax in more than one state. Caution must be observed in administering a trust to determine which state law will govern the trust and to address the relevant state income tax rules.

33. Does your jurisdiction maintain a central register of trusts?

The US does not maintain a central register of trusts.

34. Does your jurisdiction recognise trusts that are governed by another jurisdiction's laws and are created for foreign persons?

State law generally recognises the validity of trusts created by NRAs under the laws of a foreign jurisdiction.

35. What are the tax consequences of trustees (for example, of an English trust) becoming resident in/leaving your jurisdiction?

Detailed tax advice should be sought in relation to the import or export of a trust to or from the US. A number of consequences may apply. For example:

- Where a US trust becomes a foreign non-grantor trust, all of its assets may be subject to tax as if they had been sold for FMV with no offset for any loss on the date it becomes a foreign trust (*section 684, Code*). Section 684 may apply, for example, where a foreign grantor trust with respect to a US person becomes a foreign non-grantor trust (*see Question 32*).
- Taxation is not generally imposed at the point at which a foreign trust becomes a US trust. Income generated by a trust post-migration to the US is subject to US income tax. A US non-grantor trust is entitled to a deduction for income distributed to beneficiaries that is included in DNI, and to the extent that the income is distributed to an NRA, there is no US income tax on non-US source income.
- A trust which has migrated to the US is no longer subject to particular rules which apply to a foreign trust (such as filing requirements under Forms 3520 and 3520-A). It is still, however, subject to the "throwback rules", although their application is postponed (*see Question 32*).

36. If your jurisdiction has its own trust law, does the law provide specifically for the creation of non-charitable purpose trusts? Does the law restrict the perpetuity period within which gifts in trusts must vest, or the period during which income may be accumulated? Can the trust document restrict the beneficiaries' rights to information about the trust?

Purpose Trusts

In the US, the validity of trusts is determined by state law. In general, states permit the creation of trusts for non-charitable purposes, although traditionally such trusts were required to have an identifiable individual beneficiary. In recent years, several US states have expressly authorised non-charitable purpose trusts that do not require an identifiable individual beneficiary. A common use for such trusts is to own and manage an important family asset, for example, a private family trust company, without requiring the trustee to prioritise the economic interests of any class of individual beneficiaries.

Perpetuities and Accumulations

State law determines the perpetuity period within which gifts and trusts must vest and these vary among the various states, for example:

- Many states maintain the traditional rule against perpetuities derived from English law which requires vesting within lives-in-being at the time the trust becomes irrevocable, plus 21 years.
- Other states have simplified the rule against perpetuities, which may permit, for example, that the interests in trusts must vest within 90, 360 or 1,000 years from the date of creation. Examples include Florida (360 years) and Wyoming (1,000 years).
- Several states in the US have either abolished or enacted a way to elect out of the common law rule against perpetuities. These states include:

- Alaska;
- Delaware;
- Hawaii;
- Idaho;
- Illinois;
- Kentucky;
- Maine;
- Maryland;
- Michigan;
- Missouri;
- Nebraska;
- New Hampshire;
- New Jersey;
- Ohio;
- Pennsylvania;
- Rhode Island;
- South Dakota;
- Virginia; and
- Wisconsin.

- Clients wishing to create a long-term trust for their family may wish to prioritise one of these states. To ensure sufficient connections with the selected state, the trust creator would typically appoint an individual or bank/trust company resident in the state as the trustee to ensure the favorable perpetuity rules.

It should also be noted that certain states also have no state income tax on trust income. These jurisdictions may also be attractive venues for administering a trust:

- Alaska.
- Florida.
- Nevada.
- South Dakota.
- Texas.
- Washington.
- Wyoming.

Other states will not tax trusts created by NRAs even if the trust is governed by the applicable state's laws and is administered in the state.

Beneficiaries' Rights to Information

Trustees traditionally have a duty to report trust activity to beneficiaries on an annual or other periodic basis. State trust law often permits the trust settlor to waive or limit this obligation. Several states also expressly authorise "silent trusts", in which the trustee has no obligation to inform the beneficiaries of the trust's existence for a period of time.

37. Does the law in your jurisdiction recognise claims against trust assets by the spouse/civil partner of a settlor or beneficiary on the dissolution of the marriage/partnership?

The rights of spouses in trust assets are determined under state law. In general, state law recognises the validity of "spendthrift" clauses in a trust instrument and some states presume that a trust contains such a clause absent express direction to the contrary. A spendthrift clause prohibits a trust beneficiary from assigning, transferring or otherwise alienating his or her beneficial interest in the trust and, for similar reasons, prohibits a beneficiary's creditor from reaching trust assets. Nearly all trusts created for estate and tax planning purposes contain a spendthrift clause (and can be referred to as "spendthrift trusts").

In the case of spendthrift trusts created by a third party, however, a beneficiary's interest is generally not subject to claims brought by the beneficiary's spouse or civil partner. Despite this general rule, property settlements upon divorce can be determined within the broad discretion of state courts. Some courts have considered a beneficiary's trust assets when dividing up the couple's non-trust assets upon divorce or setting the amount of alimony and child support.

38. To what extent does the law of your jurisdiction allow trusts to be used to shelter assets from the creditors of a settlor or beneficiary?

State law generally recognise spendthrift trusts which prohibit a trust beneficiary's creditors from reaching the assets of the trust (*see Question 37*). However, most states historically would not recognise a spendthrift trust created by a trust settlor for his own benefit. This historical approach has been substantially modified by statute in many states, which now recognise self-settled trusts that provide creditor protection within prescribed limits. All US states forbid fraudulent transfers, which would include any transfer made to hinder, delay or avoid creditors. An individual could not, therefore, create a valid self-settled trust to avoid pre-existing creditor claims.

Most states also recognise a limited class of "exception creditors" who would still be able to reach the assets of a self-settled trust if the trust creator would otherwise be unable to pay their claims. These exception creditors might include a current or former spouse, creditors of child support obligations, certain tort victims and/or the government.

Nevertheless, most states still do not permit creditor protection for self-settled trusts created under their laws and may not respect such a trust created under another state's laws. Therefore, the practical effect of a self-settled trust in other states (which do not recognise them) may be quite limited.

CHARITIES

39. Are charities recognised in your jurisdiction?

Charities are recognised under both state and federal law.

Under state law, a charity can be established as a charitable trust or as a corporation established pursuant to state statutes of incorporation (whether under a general incorporation statute or a specific statute that expressly authorises non-profit/charitable corporations).

For both purposes, a charity must be organised and operated for one of the exempt purposes under section 501(c)(3) of the Code, which must be for a purpose that is charitable, religious,

educational, scientific, literary, testing for public safety, fostering national or international amateur sports competition, and/or preventing cruelty to children or animals.

The term "charitable" is used in its generally accepted legal sense and includes:

- Relief of the poor, distressed, or underprivileged.
- The advancement of religion.
- The advancement of education or science.
- Erecting or maintaining public buildings, monuments, or works.
- Lessening the burdens of government.
- Lessening neighbourhood tensions.
- Eliminating prejudice and discrimination
- Defending human and civil rights secured by law.
- Combating community deterioration and juvenile delinquency.

See also *Charitable Organisations in the United States (California): Overview* and *Charitable Organisations in the United States (New York): Overview.*

40. If charities are recognised in your jurisdiction, how can an individual donor set up a charity?

Every charitable organisation is generally classified as either a:

- **Private foundation.** These can be organised as either a corporation or a charitable trust. A private foundation is generally controlled by a small group of individuals and derives much of its support from a small number of sources. Private foundations are subject to various operating restrictions and to excise taxes if they fail to comply with the restrictions
- **Public charity.** These must also distribute a minimum amount for charitable purposes each year and pay a small excise tax on investment income. Public charities generally receive a greater portion of their support from the general public and have greater interaction with the public and do not have to abide by the same restrictions as private foundations (or pay the associated excise taxes).

(*Section 501(c)(3), Code*).

Any organisation established under section 501(c)(3) of the Code is presumed to be a private foundation unless it requests, and qualifies for, a ruling or determination as a public charity (qualifying organisations include churches, schools, hospitals, medical research organisations, publicly-supported organisations, donor advised funds and certain organisations operated to support other public charities).

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- Execute a trust instrument (if organised as a charitable trust).
- File articles of incorporation/formation with the state agency that oversees corporate entities (usually called a "secretary of state").

41. What are the main regulatory authorities for charitable organisations? What are their powers of investigation/audit/sanctions?

Charitable or non-profit entities are usually subject to regulation (and occasionally, to registration requirements) under the state attorney general or other law enforcement agency. Private foundations that do not fundraise from the general public are subject to much lighter regulatory regimes at the state level relative to public charities.

State attorney generals (or other state-level regulators) have the authority to audit charitable organisations and otherwise ensure that the organisations are being operated for legitimate charitable purposes.

42. What are the benefits for individuals when setting up charitable organisations?

Organisations qualifying as charities under US federal tax law receive two main benefits:

- The organisation is generally exempt from paying federal income tax on its income.
- Donors to the organisation may receive an income tax deduction in the amount of their contributions.

The availability and extent of the second benefit, which accrues to the charity's donors, may depend on the characteristics of the charity itself and of the type of property contributed by the donor, for example:

- Contributions to a public charity are deductible by the donor up to 60% of the donor's adjusted gross income. By contrast, contributions of shares or certain other appreciated property are deductible up to 30% of the donor's adjusted gross income. Any contributions in excess of that limitation may be carried forward for up to five succeeding tax years.
- Contributions to a private foundation are eligible for more restrictive benefits. Donations of special property, such as artwork, real estate and interests in trusts, are governed under even more technical rules and regulations.

Federal tax law also restricts the availability of deductions for donations to foreign charities.

In addition to income tax deduction, federal tax law also accords an estate and gift tax deduction for donations to qualified charities, whereby no gift tax is charged for lifetime gifts, nor any estate tax for testamentary gifts, to qualified charities.

43. What are the main disadvantages of setting up a charitable organisation?

The principal disadvantages of creating a charitable organisation are:

- The expenses of compliance and administration.
- The public disclosure obligations.

The creation and qualification of a charitable organisation requires the engagement of experienced counsel and the payment of various state and federal user fees. In addition, annual tax returns and other periodic regulatory filings must be prepared and submitted, which require the participation of qualified advisers or paid staff/volunteers.

Furthermore, charitable organisations are required to make certain public disclosures under federal and state law. Some states, such as New York and California, require registration in a publicly available database. US federal tax law also requires the public disclosure of private foundation tax returns, which includes disclosing information about the foundation's officers and directors, donor, assets, income and grants to other charitable organisations.

Furthermore, charitable organisations are required to make certain public disclosures under federal and state law. Some states, such as New York and California, require registration in a publicly available database. US federal tax law also requires the public disclosure of private foundation tax returns, which includes disclosing information about the foundation's officers and directors, donor, assets, income and grants to other charitable organisations.

44. What are the benefits to individual donors making donations to charitable organisations?

Under US federal law, organisations established as charities are generally exempt from paying federal income tax and donors may also be permitted to receive an income tax deduction for contributions made to the charity. The rules governing both the income tax exemption and whether an organisation would be eligible to receive tax-deductible contributions are set out in sections 501 and 170 of the Code.

State law grants various exemptions (including property tax, sales tax, filing obligations and user fees) for qualified non-profit or charitable entities. US federal tax law also exempts other non-charitable organisations (such as membership clubs, trade organizations and political action committees) from income tax, although donors are not generally permitted to deduct contributions to such organisations for income tax purposes.

In addition to income tax deductions, a donor would also be able to avoid the capital gain taxation on appreciated assets donated to a qualified charity.

OWNERSHIP AND FAMILIAL RELATIONSHIPS

Co-ownership

45. What are the laws regarding co-ownership and how do they impact on taxes, succession and estate administration?

Property co-ownership is generally determined under state law.

Joint Tenants/tenants in Common

The US states recognise a variety of co-ownership arrangements, which are traditionally based on the common law system of landed estates. This may involve either:

- Co-ownership as joint tenants with right of survivorship, in which the surviving co-owner will automatically accede to full ownership on the death of the other co-owner(s).
- Co-ownership as tenants in common, in which each co-owner's interest in the property can be transferred during life and is subject to disposition under his will.

Analogous rights exist for co-owners of bank accounts and other financial assets. Income on co-owned property is allocated among co-owners based on the ownership interest (which, in the absence of specific agreement, is presumed to be equal). For federal estate tax purposes, a co-owner's interest in the co-owned property is included in their gross estate.

Community of Property

In states that follow the civil law system of community property for married couples, the property of a married individual is presumed to be the community property of both spouses (regardless of how the property is titled). Each spouse is the beneficial owner of a one-half undivided interest in the community property, which may generally be transferred during life and subject to disposition under his will. Income on community property is generally allocated one-half to each spouse.

For federal estate tax purposes, each spouse's one-half community property interest is included in his gross estate. In addition, under the current federal tax law in effect, the entire community property receives a new tax basis on the death of the first spouse to die which is equal to the fair market value of the property at that time. This "stepped up" basis has the effect of eliminating any taxable gains in the property so that the community property can often be sold following the death without generating much (if any) income tax. However, at the time of writing, there have been several legislative proposals to eliminate "stepped up" basis for a decedent's assets.

See also *Question 46*.

Familial Relationships

46. What matrimonial regimes in trust or succession law exist in your jurisdiction? Are the rights of cohabitees/civil partners in real estate or other assets protected by law?

Matrimonial regimes, succession law and other property and family law issues are generally determined by state law.

Community of Property Regime

Several states follow the civil law system of community property for married individuals, including:

- Arizona.
- California.
- Idaho.
- Louisiana.
- Nevada.
- New Mexico.
- Texas.
- Washington.
- Wisconsin.

In addition, Alaska, South Dakota and Tennessee permit spouses to "opt in" to a community property regime.

The community property regime generally presumes the property of a married individual is community property and provides for automatic equal co-ownership rights for both spouses, regardless of how the property is titled. See also *Question 45, Community of Property.*

Separate Property Regime

The remaining states follow the common law system of separate property for married couples. The separate property regime generally presumes that the spouse who owns the property has full rights of use and disposition, both during life and at death, subject to the rights of the other spouse upon divorce and death.

State law also generally permits spouses to enter into an agreement (often called a "pre-nup" and/or "post-nup") to vary the default rules regarding joint ownership, division on divorce, and a

surviving spouse's entitlements in the estate of the deceased spouse.

47. Is there a form of recognised relationship for same-sex couples and how are they treated for tax and succession purposes?

In 1996, the US federal government passed the Defense of Marriage Act (DOMA), which restricted the definition of marriage for all federal purposes (including federal income, estate and gift tax purposes) to a union of one man and one woman. In 2013, the US Supreme Court declared those provisions of DOMA to be unconstitutional for federal law purposes.

DOMA also allowed US states to refuse to recognise same-sex marriages that were validly performed in other jurisdictions. In 2015, the US Supreme Court ruled that the US Constitution requires a state to license a marriage between two people of the same sex and to recognise a marriage between two people of the same sex when their marriage was lawfully licensed and performed in another jurisdiction.

For all federal tax purposes, a marriage between a same-sex couple that is valid under state law is treated identically to a marriage between one man and one woman.

48. How are the following terms defined in law: married, divorced, adopted legitimate, civil partnership?

Married

The definition of this term is governed by state law.

Divorced

The definition of this term is governed by state law.

Adopted

The definition of this term is governed by state law. Under the laws of most US states, adopted children are treated in an equivalent manner as biological children (although for trusts created many years ago, these rules sometimes do not apply, and adopted children may not always be treated in an equivalent manner).

Legitimate

The definition of this term is governed by state law. Most states have eliminated any meaningful distinction between legitimate and illegitimate children for most trust, estate and other property law purposes.

Civil Partnership

The definition of this term is governed by state law.

Minority

The definition of this term is governed by state law. US states generally recognise 18 years as the age of majority for most purposes.

49. What rules apply during the period when an heir is a minor? Can a minor own assets and who can deal with those assets on the minor's behalf?

State law, which governs questions of capacity and property ownership, generally does not permit minors to own substantial property in their individual names. For example, if a minor accedes to a large inheritance from an estate, the court will usually require the appointment of a guardian for their property.

Furthermore, in the course of a probate proceeding, minors are often deemed incapable of representing their own interest and the court may require the appointment of a guardian ad litem (to act on their behalf) to ensure fairness and avoid any conflicts of interest with other interested parties (for example, the minor's parents who may also be estate beneficiaries).

CAPACITY AND POWER OF ATTORNEY

50. What procedures apply when a person loses capacity? Does your jurisdiction recognise powers of attorney (or their equivalent) made under the law of other jurisdictions?

State law determines whether an individual has capacity to make financial and other decisions on his own behalf.

All states recognise a "durable" power of attorney in which an individual (called the "principal") may execute to nominate an agent to make financial decisions if and when he or she later becomes incapacitated. A power of attorney may also authorise an agent to make these decisions [##long-term even after the principal has retained capacity.]

The formalities and other requirements for a valid power of attorney also vary by state, but most states will recognise the validity of a power of attorney executed in compliance with the requirements of the place where it was executed and/or the place of the principal's domicile at the time of execution.

If an incapacitated individual does not have a valid power of attorney, state law generally requires the appointment of a guardian (also sometimes called a "conservator") to make decisions on the individual's behalf.

PROPOSALS FOR REFORM

51. Are there any proposals to reform private client law in your jurisdiction?

Unless the US federal government takes additional action, the TCJA will sunset on 1 January 2026, returning the current USD11.7 million applicable exclusion amount to its previous, lower level (*see Question 8*).

At the time of writing, President Biden and Democratic members of Congress have proposed various possible changes to the wealth transfer tax regime at the federal level. Such proposals include, among other fundamental changes:

- Reducing the applicable exclusion amounts to below the pre-TCJA levels.
- Increasing the applicable estate and gift tax rates.

However, it is much too early to speculate on the likelihood of any such proposal being ultimately enacted into law and the associated implications.

Practical Law Contributor Profiles

Jennifer Jordan McCall

Pillsbury Winthrop Shaw Pittman LLP

T +1 650 233 4020
F +1 650 233 4545
E mccall@pillsburylaw.com
W www.pillsburylaw.com

Professional Qualifications. New York, US, 1983; California, US, 2002; Florida, US, 2014

Areas of Practice. Estates; trusts and tax planning.

Recent Transactions

- Representing individuals, families, foundations, museums and charities regarding domestic and international gift and estate planning.
- Advising clients with respect to estate, gift and generation-skipping transfer taxes, complex estate administration, estate-related litigation, and the integration of these matters with the client's business objectives.

Christopher B Lacaria

Pillsbury Winthrop Shaw Pittman LLP

T +1 212 858 1103
E christopher.lacaria@pillsburylaw.com
W www.pillsburylaw.com

Professional Qualifications. New York, US, 2014

Areas of Practice. Estates; trusts and tax planning.