

ISSUE #5
February 2007



MATSUMURA LAW FIRM

Wills, Trusts, Probate
And Estate Planning

U.S. Residency Subjects A Non-Citizen Spouse to U.S. Estate and Gift Taxes

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Estate Planning for Non-U.S. Citizens:

Estate and Gift Tax Considerations for Non-Citizen Spouses

Estate planning for non-U.S. citizens (i.e., aliens) involves a variety of complex issues. This month's newsletter hopefully provides some basic estate planning considerations specific to aliens. This discussion will focus on issues for non-citizen *spouses*.

1. The Residency Test. First of all, it is important to distinguish between a non-resident alien and a

resident alien for tax purposes. Non-citizen residents are subject to estate and gift taxes on their worldwide assets. The residency test for U.S. estate tax purposes is a domicile test, based upon all the facts and circumstances. Visa status and the number of days spent in the U.S. are relevant but not determinative. Sometimes it is very clear that an alien is a resident of the U.S.—i.e., she has lived in the U.S. for a number of years, her spouse and children are U.S. citizens and her contacts (doctors, financial advisors, and other relationships) are all within the U.S. However, if the facts are not as clear, it may be prudent to consult an international attorney to verify what the foreign country's laws would conclude.

2. Estate Tax Exemption Amount Available. If a alien is a U.S. resident, she is entitled to

the full estate tax exemption amount (for 2007 and 2008, the amount is \$2,000,000).

3. No Estate Tax Marital Deduction—QDOT Trust Required. If both spouses are U.S. citizens, the estate tax marital deduction rule allows each spouse to leave an unlimited amount of property to the other spouse without any estate tax consequences. As a result, citizen spouses never have to bear estate tax liability upon the death of a first spouse.

However, the benefit of the unlimited marital deduction is available only if the recipient spouse is a U.S. citizen. If the recipient spouse is not a U.S. citizen, *if no other planning is done*, the IRS will tax amounts passing to that spouse which are not otherwise sheltered by the estate tax exemption. In other words, a U.S. citizen spouse can leave an estate tax exemption amount to the non-citizen spouse and any property above that threshold will need further estate planning to minimize tax. Any excess property must be left in a Qualified Domestic Trust (QDOT) trust which will postpone the estate tax on those assets until the death of the non-citizen spouse.

A QDOT must provide that (1) at least one trustee is a U.S. citizen; (2) the trust principal is distributed to the non-citizen spouse only subject to estate tax at the decease spouse's rate; (3) upon the non-

(continued on reverse)

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Estate Planning for Non-U.S. Citizens (continued)

citizen spouse's death, the trust balance is subject to estate tax at the deceased spouse's estate tax rate. There is a *hardship exception* to exempt principal distributions from estate tax, but this exception is only available if the non-citizen spouse has insufficient income or other assets to meet basic needs.

If the non-citizen spouse becomes a U.S. citizen during the term of the QDOT, the principal of the QDOT can be distributed free of estate tax.

4. No Unlimited Lifetime Gifts Exemption to Non-U.S.

It should be noted that joint tenancies between spouses (where one spouse is a non-citizen) are also treated differently than if both spouses are U.S. citizens. If both spouses are citizens, when one spouse passes away, only one-half of the joint property is included in the gross estate of the deceased spouses. In contrast, if the citizen spouse is the first to pass away, the *entire value of all joint property* is included in the citizen's gross estate for estate tax purposes. The non-citizen spouse has the burden of proving that he or she contributed to the acquisition cost of the joint property.

As illustrated above, estate planning

“Planning is Required: No Unlimited Marital Deduction is Available to Non-Citizen Spouses.”

Citizen Spouses. For spouses who are both U.S. citizens, one spouse may make an unlimited amount of gifts to the other spouse without gift tax consequences. However, if the donee spouse is not a U.S. citizen, then only an annual exclusion amount of \$125,000 (2007) may be gifted to that non-citizen spouse. Any gifts in excess of this amount will be subject to gift tax, against which the donor spouse must apply unused portion of his or her estate tax exemption amount.



for non-U.S. citizens require special attention. Once a non-citizen is a “resident” of the U.S., many tax consequences follow. *

Estate Planning Definition:

Issue—means not only a person's children, but also any grandchildren and great-grandchildren (i.e., all of the person's direct descendants, including adopted children).

About Me

I graduated cum laude from the University of the Pacific in Stockton, California in Business and received my law degree (J.D.) from King Hall School of Law at U.C. Davis. I was admitted to the California State Bar in 1993 and completed my Masters in Taxation (LL.M.) at Golden Gate University in 1998.

I have practiced exclusively in the area of estate planning, pro-

trust administration for approximately nine years. My main office is in Pleasanton, but I often travel to homes or other locations to make the process of estate planning easier for my clients.

In my non-work hours, I support the University of California Athletics, the San Francisco Giants, the Sacramento Kings, and play tennis! **GO BEARS!**

Next Issue: Using Life Insurance Trusts To Avoid Paying Policy Proceeds to Uncle Sam