Estate and Gift Taxes for Nonresident Aliens

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Summary

This report explains the major provisions of the federal estate and gift transfer taxes as they apply to transfers by nonresident aliens in 2014. Estate and gift taxes are two federal transfer taxes imposed on the passing of property title from one person or entity to another. The federal estate tax is levied on the transfer of property at death, while the federal gift tax is levied on the transfer of property during life by one individual to another while receiving nothing or less than full value in return. The following discussion provides basic principles regarding the computation of these two transfer taxes for this particular group of taxpayers.

In determining estate and gift tax liability, the Internal Revenue Code (IRC) differentiates between the estates of citizens, resident aliens, and nonresident aliens. Under the estate tax regulations, a “resident” decedent is a decedent who, at the time of his death, had his domicile in the United States. A person acquires a domicile in a place by living there, for even a brief period of time, with no definite present intention of later leaving that place. The estates of resident aliens follow the same rules and regulations as do the estates of U.S. citizens to determine estate tax liability. However, the estates of nonresident aliens are taxed differently.

The federal estate tax is measured by the size of the decedent’s estate. The tax is computed through a series of adjustments and modifications of a tax base known as the “gross estate.” Unlike the estates of U.S. citizens, the gross estates of nonresident aliens include only property “situated” in the United States. Certain allowable deductions reduce the gross estate to the “taxable estate,” to which is then added the total of all lifetime taxable gifts made by the decedent. Estates of citizens, resident aliens, and nonresident aliens share many deductions, including estate administration expenses, certain debts and losses, charitable bequests, and the amount of qualified transfers to a surviving spouse, although estates of nonresident aliens calculate some deductions differently. The tax rates are applied and, after reduction for certain allowable credits, the amount of tax owed by the estate is reached.

The federal gift tax for nonresident aliens is a tax imposed on gratuitous transfers of U.S. real estate and tangible personal property situated in the United States during life. The tax seeks to account for transfers of property that would otherwise reduce the estate and accordingly estate tax liability at death. The donor’s tax liability of the gift depends upon the value of the “taxable gift.” The taxable gift is determined by reducing the gross value of the gift by the available deductions and exclusions. The major deductions and exclusions available for nonresident donors are the annual exclusion, the gift tax marital deduction, and the gift tax charitable deduction.
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his report explains the major provisions of the federal estate and gift transfer taxes for transfers by nonresident aliens in 2014. This discussion highlights the different tax rules for estates of nonresident aliens as compared to the estates of U.S. citizens and resident aliens.

In determining estate tax liability, the Internal Revenue Code (IRC) differentiates between the estates of U.S. citizens, resident aliens, and nonresident aliens. The estates of resident aliens follow the same rules and regulations to determine estate tax liability as do estates of U.S. citizens. However, the estates of nonresident aliens are taxed differently. This report will focus on the estate tax rules for this particular group of taxpayers.

Department of the Treasury (Treasury) regulations define a “nonresident alien” for the purposes of the estate and gift taxes. However, other areas of the law, including income tax law, do not rely on the same definition or terminology for a “nonresident alien.” This report will use the definition for U.S. citizens, resident aliens, and nonresident aliens found in the Treasury regulations’ estate tax provisions.

Determining the final estate tax liability of a resident or nonresident alien ultimately relies upon the citizenship of the decedent and whether the United States has signed an estate tax treaty with that country. These estate tax treaties alter some aspects of the U.S. federal estate tax rules discussed in this report. Even if a noncitizen-decedent is considered a U.S. resident under the IRC, an estate tax treaty may classify the decedent as a nonresident alien for U.S. estate tax purposes. This report will briefly discuss the implications of tax treaties on the treatment of estate and gift taxes for nonresident aliens, but will not address individual estate and gift tax requirements under each treaty.

In order to understand the key differences between estate and gift tax liability for U.S. citizens, resident aliens, and nonresident aliens, this report will first discuss the definition of “nonresident alien” under the Treasury’s estate and gift tax regulations. Next, the report will explain the estate tax requirements under the IRC for nonresident aliens and the necessary steps to calculate estate tax liability. Because the federal estate and gift taxes for U.S. citizens, resident aliens, and nonresident aliens are unified and use the same rate structure, the report will address the gift tax for nonresident aliens and the procedures used to calculate this tax. The report will conclude with a chart summarizing the differences regarding the tax treatment among estates of U.S. citizens, resident aliens, and nonresident aliens.

Definition of a Nonresident Alien

Under the estate tax regulations, a “resident” decedent is a decedent who, at the time of his death, had his domicile in the United States. A person acquires a domicile in a place by living there, for

1 For more information on the definition of “nonresident alien” in estate and income taxes, see CRS Legal Sidebar WSLG729, A Story In Inconsistency: The U.S. Tax Code’s Definition of Resident Aliens, by Emily M. Lanza and Erika K. Lunder.


even a brief period of time, with no definite present intention of later leaving that place. A person’s residence will not qualify as a domicile unless the person has the requisite intent to remain in such residence indefinitely. An intention to change domicile will not generate such a change unless accompanied by actual removal; intent to leave is not sufficient. A nonresident alien, for purposes of the estate tax, is an individual who, at the time of his death, had his domicile, as defined above, outside of the United States. An individual who is present in the United States on a nonimmigrant visa can be considered a resident for estate and gift tax purposes if the individual wants to permanently remain in the United States even though the visa does not allow permanent residence.

Because the determination of a person’s “domicile” relies upon the intent of an individual, a bright-line test to determine if an individual is a resident for federal estate and gift tax purposes is not available. Therefore, the courts consider the following factors in making such a determination: visas, work permits, location of business and property interests, family immigration history, residential property, individual testimony, motivation, duration of stays in the United States, and community group affiliations.

**Estate Tax for Nonresident Aliens**

The federal estate tax is a tax on the estate of a decedent, levied against and paid by the estate. The determination of federal estate tax liability involves a series of adjustments and modifications of a tax base known as the “gross estate.” Certain allowable deductions reduce the gross estate to the “taxable estate.” Then, the total of all lifetime taxable gifts made by the decedent is added to the taxable estate before tax rates are applied. The result is the decedent’s estate tax which, after the reduction for certain allowable credits, is the amount of tax paid by the estate.

**The Gross Estate: The Federal Estate Tax Base**

The first step in determining estate tax liability for citizens, resident aliens, and nonresident aliens is to designate the “gross estate,” which consists of property in which the decedent held an interest at the time of death. However, the gross estates of nonresident aliens, for federal estate tax purposes, include only property “situated” in the United States. Real property and tangible personal property physically located in the country qualify as property “situated” in the United States. Shares of stock issued by a corporation incorporated in the United States, regardless of the physical location of the certificates, and debt obligations of U.S. persons or political subdivisions are also “situated” in the United States. Certain types of property, such as works of

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4 Id.
art imported or loaned for exhibition purposes, are not considered to be “situated” in the United States for the purposes of defining the gross estate.11

Like the estates of citizens and resident aliens, the value of the nonresident alien’s gross estate is based on the fair market value of the decedent’s estate at the date of death. Fair market value is the price at which the estate property would change hands between a willing buyer and seller.12 An alternative valuation date of six months following the date of death may be used if the value of the estate is reduced between date of death and the alternate date.

Nonresident alien estates of more than $60,000 in U.S. gross assets must file a federal estate tax return.13

**Deductions from the Gross Estate: Reaching the Taxable Estate**

A decedent’s taxable estate is determined by reducing the gross estate with allowable deductions. Estates of citizens, resident aliens, and nonresident aliens share many deductions, including estate administration expenses, certain debts and losses, charitable bequests, and the amount of qualified transfers to a surviving spouse, although some differences in calculating these deductions may apply.

Estates of nonresident aliens may deduct a portion of certain expenses and losses, such as funeral and administration expenses and debts with respect to property included in the gross estate.14 The portion of these expenses that a nonresident alien’s estate may deduct is determined by the proportion of the value of the gross estate situated in the United States to the value of all estate property, wherever situated.15 Whether the decedent incurred the debt or loss in the United States is irrelevant for the purposes of this deduction. Estates of nonresident aliens may also deduct charitable contributions to a U.S. government entity for exclusively public purposes, a U.S. charitable corporation, a charitable trust that uses the gift for its charitable purposes within the United States, and certain U.S. fraternal societies.16

Like the estates of citizens and resident aliens, the estate of a nonresident alien may deduct from the gross estate the value of property passing to the decedent’s surviving spouse, under certain circumstances.17 If the surviving spouse is a U.S. citizen at the time of the decedent’s death, a marital deduction18 is allowed if the other requirements outlined in IRC’s Section 2056 are

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18 The Economic Recovery Tax Act of 1981 provided an unlimited marital deduction for property passing to the surviving spouse regardless of citizenship. This created an opportunity for a noncitizen spouse to avoid paying U.S. estate taxes on the citizen spouse’s property by returning to their native country after a citizen spouse’s death. In response to this issue, Congress passed the Technical and Miscellaneous Revenue Act of 1988, which repealed that particular estate tax marital deduction for property passing to noncitizen spouses.
satisfied.\textsuperscript{19} Section 2056 forbids the marital deduction if the interest in property that is being passed to the spouse would terminate on the occurrence or non-occurrence of an event; if another interest in that property has passed for full consideration in money; and if a third person may possess an interest in the property after the termination of the spouse’s interest.\textsuperscript{20} These rules apply to the estates of citizens and resident aliens as well.

If the surviving spouse is not a U.S. citizen (regardless of whether he or she resides in the United States),\textsuperscript{21} the bequest to the surviving spouse will not qualify for the marital deduction unless the property is held in a qualified domestic trust (QDOT)\textsuperscript{22} or unless the surviving spouse becomes a U.S. citizen within a specified period after the decedent spouse’s death.\textsuperscript{23}

The purpose of the QDOT is to ensure the payment of the federal estate tax that was deferred on the death of the first spouse through the marital deduction because of the possibility that the surviving noncitizen spouse’s estate will not be subject to the federal estate tax.\textsuperscript{24} A QDOT must have at least one U.S. trustee who is an individual citizen or a domestic corporation and has veto power over distributions from the trust.\textsuperscript{25} The trust instrument of a QDOT must prevent distributions from the trust unless a U.S. trustee has the right to withhold estate tax imposed on the distribution.\textsuperscript{26} If the assets passing to the QDOT exceed $2 million, the U.S. trustee for the QDOT must either be a bank or must furnish a bond or letter of credit.\textsuperscript{27}

The estate’s executor must make an election to apply the QDOT rules.\textsuperscript{28} The estate tax is payable on a taxable event, which includes principal distributions from the QDOT to the surviving noncitizen spouse.\textsuperscript{29} The balance of the trust value is taxed at the noncitizen spouse’s death.\textsuperscript{30} The estate tax is calculated based on the decedent’s tax brackets and can account for the decedent’s taxable gifts and other adjustments.\textsuperscript{31}

A QDOT is not necessary if the surviving spouse is a U.S. citizen before the decedent’s estate tax return is due as long as the spouse resided in the United States after the decedent’s death and before becoming a U.S. citizen.\textsuperscript{32}

\textsuperscript{20} 26 U.S.C. §2056.
\textsuperscript{21} Unlike the broader estate tax, the marital deduction does not use the “domicile test.” Whether a spouse receives the marital deduction depends on whether he/she is a citizen or not. A noncitizen spouse can be a resident or nonresident alien.
\textsuperscript{22} Sometimes abbreviated as “QDT.”
\textsuperscript{24} \textit{See also} Diana S.C. Zeydel and Grace Chung, “Estate Planning for Noncitizens and Nonresident Aliens: What Are Those Rules Again?”\textsuperscript{106} JTAX 20, 22 (2007).
\textsuperscript{26} \textit{Id.}
\textsuperscript{27} Treas. Regs. (26 C.F.R.) §20.2056A-2(d).
\textsuperscript{29} 26 U.S.C. §2056A(b)(3)(B).
\textsuperscript{30} 26 U.S.C. §2056A(b).
\textsuperscript{31} \textit{Id.}
\textsuperscript{32} 26 U.S.C. §2056(d)(4).
Computation of the Estate Tax

Like the estates of citizens and resident aliens, estates of nonresident aliens are subject to the unified estate and gift tax system. Therefore, computation of the nonresident alien’s estate tax liability requires a “grossed-up” or a combination of the decedent’s lifetime taxable gifts and the decedent’s taxable estate to which the tax rate schedule is then applied. Any available credits are subsequently taken to obtain the decedent’s actual estate tax liability (the amount of tax to be paid by the estate).33

Estates of U.S. citizens, resident aliens, and nonresident aliens share the same estate tax rate schedule34 as follows:

<table>
<thead>
<tr>
<th>Taxable Estate</th>
<th>Tentative Tax</th>
</tr>
</thead>
<tbody>
<tr>
<td>not over $10,000</td>
<td>18% of such amount</td>
</tr>
<tr>
<td>$10,000-$20,000</td>
<td>$1,800 + 20% of excess over $10,000</td>
</tr>
<tr>
<td>$20,000-$40,000</td>
<td>$3,800 + 22% of excess over $20,000</td>
</tr>
<tr>
<td>$40,000-$60,000</td>
<td>$8,200 + 24% of excess over $40,000</td>
</tr>
<tr>
<td>$60,000-$80,000</td>
<td>$13,000 + 26% of excess over $60,000</td>
</tr>
<tr>
<td>$80,000-$100,000</td>
<td>$18,200 + 28% of excess over $80,000</td>
</tr>
<tr>
<td>$100,000-$150,000</td>
<td>$23,800 + 30% of excess over $100,000</td>
</tr>
<tr>
<td>$150,000-$250,000</td>
<td>$38,800 + 32% of excess over $150,000</td>
</tr>
<tr>
<td>$250,000-$500,000</td>
<td>$70,800 + 34% of excess over $250,000</td>
</tr>
<tr>
<td>$500,000-$750,000</td>
<td>$155,800 + 37% of excess over $500,000</td>
</tr>
<tr>
<td>$750,000-$1,000,000</td>
<td>$248,300 + 39% of excess over $750,000</td>
</tr>
<tr>
<td>Over $1,000,000</td>
<td>$345,800 + 40% of excess over $1,000,000</td>
</tr>
</tbody>
</table>

Source: Congressional Research Service

The following tax credits are available for estates of nonresident aliens: unified transfer tax credit, state death tax credit, and credit for tax on prior transfers.35

The unified transfer tax credit is available against both lifetime gift tax liabilities and the estate tax liability. To the extent this credit is used to offset gift taxes, it is unavailable to offset estate taxes. The IRC refers to the credit as an “applicable exclusion amount”; that is, the amount of taxable gifts or estate that the credit would cover.36 Estates of nonresident aliens are entitled to a credit of $13,000.37 Estates of nonresident aliens may apply this credit against their estate tax

34 26 U.S.C. §2001(c). The taxable estate is the gross estate less any relevant deductions. The tax rate is then applied to the taxable estate resulting in the tentative tax. Any available credits are then taken from the tentative tax to arrive at the estate’s actual tax liability.
liability, as determined in the chart above, which effectively eliminates estate tax on the first $60,000 of assets.\(^{38}\)

If a foreign tax treaty obligation is applicable, the estates of nonresident aliens are entitled to a unified credit of $192,800 multiplied by the proportion of the decedent’s gross estate situated in the United States to the total gross estate wherever situated.\(^{39}\)

The state death tax credit for nonresident aliens follows the rates outlined in IRC Section 2011 for the estates of citizens and resident aliens, but is further adjusted with the percentage of the decedent’s property on which the state death tax was actually paid against the value of the total gross estate.\(^{40}\)

Estates of nonresident aliens may also claim a credit for tax on prior transfers.\(^{41}\) The amount of this credit is determined in the same manner as that prescribed for estates of citizens and resident aliens. The credit for tax on prior transfers seeks to reduce the impact of taxes imposed on successive deaths within a short period of time. The credit applies to estate tax paid on a prior transfer of property to the decedent if the property was transferred by another person who died within 10 years before or within 2 years after the decedent.\(^{42}\)

The estate of a nonresident alien may also be eligible for tax credits available to estates of U.S. citizens/resident aliens if the nonresident decedent was a citizen of a country with which the United States has entered into an estate tax treaty requiring such obligations.\(^{43}\) The estate calculates the credit according to the proportion of the gross estate situated in the United States at time of death.

### The Federal Gift Tax for Nonresident Aliens

The federal gift tax is a tax imposed on an annual basis on all gratuitous transfers of property made during life. The tax seeks to account for transfers of property that would otherwise reduce the estate and accordingly estate tax liability at death.\(^{44}\) The donor’s tax liability on the gift depends upon the value of the “taxable gift.” The taxable gift is determined by reducing the gross value of the gift by the available deductions and exclusions. The gift tax liability created on the basis of the donor’s taxable gifts may be reduced by the available unified transfer tax credit.

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\(^{38}\) 26 U.S.C. §2102(b); Treas. Regs. (26 C.F.R.) §20.2102-1(c). The corresponding unified tax credit amount in 2014 for estates of citizens and residents is $5,340,000.


\(^{40}\) Treas. Regs. (26 C.F.R.) §20.2102-1(b).


\(^{44}\) The word “gift” is not defined in the Internal Revenue Code, but the statute does state that the amount of a gift is ascertained when “property is transferred for less than an adequate and full consideration in money or money’s worth.” 26 U.S.C. §2512(b). Generally, IRS regulations state that a gift is made, for gift tax purposes, when there is a transfer for inadequate consideration and the transaction does not take place in a business context. Treas. Regs. (26 C.F.R.) §25.2511. Other parts of the IRC do not necessarily use the same definition of “gift.”
The Taxable Gift

Nonresident aliens are subject to the federal gift tax only on gifts of their interest in U.S. real estate and tangible personal property situated in the United States.\(^{45}\) Generally, gifts of intangible property, regardless of the location of the property, made by a nonresident alien are not subject to the federal gift tax.\(^{46}\)

Citizen, resident alien, and nonresident alien donors calculate gift tax liability by first determining the amount of the taxable gift. The amount of the taxable gift is the fair market value of the gift at the time it was made, less certain exclusions and deductions.\(^{47}\) The major deductions and exclusions available for nonresident alien donors are the annual exclusion, the gift tax marital deduction, and the gift tax charitable deduction.

Like citizens and residents, a nonresident alien donor may claim an annual exclusion for transfers of a present interest in property.\(^{48}\) For transfers in 2014, the annual exclusion amount is $14,000.\(^{49}\) Therefore, in 2014, transfers by a nonresident donee within the United States that do not exceed $14,000 per donee would be excluded from the federal gift tax.

To the same extent as U.S. citizen and resident alien donors, a nonresident alien donor may claim an unlimited marital deduction of transfers of property to his or her spouse, if such spouse is a U.S. citizen.\(^{50}\) If the spouse is not a U.S. citizen, gifts to the spouse are not deductible but are eligible for a spousal “annual exclusion” indexed for inflation ($145,000 in 2014).\(^{51}\) The tax benefit that allows married couples to double the annual exclusion amount through “gift-splitting,” an arrangement in which one spouse consents to be treated as having made one-half of the gifts made by his or her spouse in that taxable year, is not available to nonresident alien donors or citizen donors with noncitizen spouses.\(^{52}\)

Like citizen donors, nonresident aliens may deduct gifts of charitable contributions. The deduction is available for gifts to a U.S. government entity for exclusively public purposes; a U.S. corporation organized exclusively for religious, charitable, scientific, literary, or educational purposes;\(^{53}\) or a charitable trust that uses the gift for its charitable purposes within the United States, certain U.S. fraternal societies, and U.S. war veterans’ organizations.\(^{54}\)

\(^{45}\) 26 U.S.C. §§2501, 2511.
\(^{48}\) 26 U.S.C. §2503(b).
\(^{50}\) 26 U.S.C. §2523(a).
\(^{51}\) 26 U.S.C. §2523(i).
\(^{52}\) 26 U.S.C. §2513.
\(^{53}\) The requirement that the corporation is “domestic” is not applicable to the gift tax charitable deduction for citizens or residents. See 26 U.S.C. §2522(a).
\(^{54}\) 26 U.S.C. §2522(b).
Computation of the Gift Tax

A nonresident alien donor follows the same guidelines for determining gift tax liability as citizen/resident alien donors. The tax liability of a taxable gift is measured initially by the value of the transferred property. The tax is then applied cumulatively to taxable gifts made over the donor’s lifetime.

The actual computation of the gift tax for each calendar year is completed in three steps. First, the donor’s taxable gifts for the calendar year and any preceding calendar years are totaled and the tentative tax determined. Second, the tentative tax is again calculated using the total taxable gifts for the preceding calendar years. Third, the result from step two is subtracted from the result of step one, and the donor’s unused unified tax credit is applied to the remaining amount.

### Table 1. Summary of Estate and Gift Tax Differences for U.S. Citizens, Resident Aliens, and Nonresident Aliens

<table>
<thead>
<tr>
<th>Decedent/ Surviving Spouse</th>
<th>Gross Estate</th>
<th>Estate Tax Applicable Exclusion Amount</th>
<th>Estate Tax Marital Deduction</th>
<th>Annual Gift Tax Exclusion Amount</th>
<th>Annual Marital Gift Tax Deduction</th>
</tr>
</thead>
<tbody>
<tr>
<td>U.S. Citizen/U.S. Citizen</td>
<td>All property wherever situated</td>
<td>$5,340,000</td>
<td>Unlimited</td>
<td>$14,000</td>
<td>Unlimited</td>
</tr>
<tr>
<td>U.S. Citizen/Resident Alien</td>
<td>All property wherever situated</td>
<td>$5,340,000</td>
<td>Only with a QDOT</td>
<td>$14,000</td>
<td>$145,000</td>
</tr>
<tr>
<td>U.S. Citizen/Nonresident Alien</td>
<td>All property wherever situated</td>
<td>$5,340,000</td>
<td>Only with a QDOT</td>
<td>$14,000</td>
<td>$145,000</td>
</tr>
<tr>
<td>Resident Alien/U.S. Citizen</td>
<td>All property wherever situated</td>
<td>$5,340,000</td>
<td>Unlimited</td>
<td>$14,000</td>
<td>Unlimited</td>
</tr>
<tr>
<td>Resident Alien/Resident Alien</td>
<td>All property wherever situated</td>
<td>$5,340,000</td>
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<td>$145,000</td>
</tr>
<tr>
<td>Resident Alien/Nonresident Alien</td>
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<td>Only with a QDOT</td>
<td>$14,000</td>
<td>$145,000</td>
</tr>
<tr>
<td>Nonresident Alien/U.S. Citizen</td>
<td>Property &quot;situated&quot; in the United States</td>
<td>$13,000</td>
<td>Unlimited</td>
<td>$14,000</td>
<td>Unlimited</td>
</tr>
<tr>
<td>Nonresident Alien/Resident Alien</td>
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<td>$145,000</td>
</tr>
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</table>

**Source:** Congressional Research Service

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