

# Nonresident Alien Estates, 1986

By DeWitt Long\*

The United States imposes an estate tax based on the portion of the estate of a nonresident alien that is located within the United States. Total gross U.S. estate of \$62.0 million and total U.S. estate tax after credits of \$6.5 million was reported for the estates of nonresident aliens who died during 1986.

## TAXATION OF THE ESTATES OF NONRESIDENT ALIENS

The United States imposes an estate tax on the estates of nonresident aliens. A nonresident alien is an individual who is not a citizen or resident of the United States at the time of the individual's death. For estate tax purposes, residency is equated with domicile, i.e., the individual's permanent home [1]. For a place to qualify as a decedent's domicile, the decedent prior to death must have been physically present there. Further, the decedent must have had no present intent to move from the place. The determination of a decedent's domicile involves an examination of the totality of the decedent's lifestyle to see whether it was centered in the United States or some other place. Among the factors considered are the location of the decedent's family, friends, and religious and social affiliations; the size, cost and location of the decedent's personal residence; the location and the type of business the decedent was engaged in; and the duration and purpose of any time that the decedent spent in the United States [2]. In addition to these factors, the decedent's immigration status is usually considered, although this factor alone is not determinative [3]. Also, the provisions of an applicable estate tax treaty with another country may affect the determination of estate tax residency [4].

In general, the estate of a nonresident alien decedent is taxed on that portion of the alien's gross estate located in the United States [5]. Gross U.S. estate is that part of the nonresident alien's gross estate (determined under Code section 2031) that is located in the United States at the time of the nonresident alien's death, and generally

includes all the nonresident alien's property [6]. The location of property is determined under several general and specific situs rules. Both real property and tangible personal property are sited to the physical location of the property. For example, real estate located in the United States owned by the nonresident alien is included in the decedent's gross U.S. estate, but real estate located outside the United States is not. Intangible property, such as a patent or a copyright, is sited to the location of the person who issues the intangible or against whom the rights to the intangible can be enforced [7]. An interest in a trust or estate is generally sited to the location of the underlying assets [8].

In addition to the general situs rules, the Internal Revenue Code contains special rules for determining the location of particular types of property. Under Code section 2104, property within the United States includes stock issued by a U.S. corporation [9]. Also, U.S. property includes any property that was transferred by the decedent in a way that would require inclusion of the property in the decedent's gross estate under the provisions of Code sections 2035, 2036, 2037 and 2038, provided that the property was located in the United States at either the time of transfer or the time of the decedent's death [10]. In addition, property within the United States includes the debt obligations of a U.S. person or governmental entity, and deposits in a U.S. branch of a foreign commercial bank [11,12].

Code section 2105 enumerates certain types of property owned by a nonresident alien decedent; considered to be located outside the United States. Property located outside the United States includes proceeds payable under an insurance policy on the life of the decedent, certain types of debt obligations, and works of art on loan for exhibition to a public gallery or museum at the time of the decedent's death [13,14].

The U.S. estate tax is imposed on the decedent's taxable estate. Taxable estate is determined by reducing

\*Foreign Returns Analysis Section. Prepared under the direction of Chris Carson, Chief.

the nonresident alien's gross U.S. estate by any allowable deductions [15]. Several types of deductions are allowed to the estates of nonresident aliens. The estate may deduct the same expenses allowed estates of U.S. citizens and residents under Code sections 2053 and 2054. Deductible expenses allowed under Code section 2053 include funeral expenses, administration expenses, claims against the estate, and indebtedness on property (where the total value of the property is included in gross estate). To be deductible, these expenses must be allowed to the estate under the law of the jurisdiction where the estate is administered [16]. Under Code section 2054, the estate can deduct losses incurred during the settlement of the estate from casualty or theft. In computing the allowable deduction for expenses under Code sections 2053 and 2054, the estate must limit the deduction to the ratio that gross U.S. estate bears to gross worldwide estate [17].

In addition to the deduction for expenses under Code sections 2053 and 2054, the estate of a nonresident alien who died during 1986 is allowed a deduction for charitable transfers under Code section 2106(a)(2). The estate can deduct contributions made to public entities or to qualifying U.S. organizations, that meet the tax-exempt requirements of Code section 501(c)(3). Also, in certain cases, a nonresident alien's estate is allowed a deduction for certain transfers of property to the alien's spouse [18].

While the estate tax is imposed on the decedent's taxable estate, the amount of the estate tax is determined by calculating the amount of tax on the sum of the decedent's taxable estate and "adjusted taxable gifts" minus the amount of estate tax on adjusted taxable gifts [19]. The tax rates, which appear in Figure A, are progressive, ranging from 6 percent on amounts less

**Figure A.--U.S. Estate Tax Schedule for Nonresident Aliens, 1986**

Amount on which tax is computed	Amount of tax
\$100,000 or less.....	6 percent of amount
Over \$100,000 to \$500,000.....	\$6,000 plus 12 percent of excess over \$100,000
Over \$500,000 to \$1,000,000.....	\$54,000 plus 18 percent of excess over \$500,000
Over \$1,000,000 to \$2,000,000.....	\$144,000 plus 24 percent of excess over \$1,000,000
Over \$2,000,000.....	\$384,000 plus 30 percent of excess over \$2,000,000

than \$100,000 to 30 percent on amounts in excess of \$2 million.

The estate of a nonresident alien could reduce its estate tax by claiming several credits. First, the estate could claim a "unified credit" of up to \$3,600. This credit served to effectively exempt estates from the U.S. estate tax if the taxable estate was less than \$60,000 [20]. Also,

the nonresident alien's estate could claim those credits allowed the estates of U.S. citizens and residents under Code sections 2011, 2012, and 2013. Code section 2011 allows a limited credit for State death taxes paid. State death taxes include any estate, inheritance, legacy, or succession tax paid to any State or the District of Columbia on property that was included in gross U.S. estate [21]. Code section 2012 allows a limited credit for taxes paid on gifts when the value of the gifts must be included in gross U.S. estate [22]. Code section 2013 allows a limited credit for taxes on prior transfers, that is, for the Federal estate tax paid on the transfer of property to the decedent by another person who died within 10 years before or 2 years after the decedent.

### ESTATE TAXATION OF U.S. CITIZENS AND RESIDENTS AND NONRESIDENT ALIENS

Several major differences exist between the taxation of the estates of nonresident aliens and the estates of citizens and residents of the United States. First, the estate of a U.S. citizen or resident is taxed on its worldwide property, whereas the estate of a nonresident alien is taxed, in general, only on that property located within the United States at the time of death [23].

A second major difference relates to the rate of tax imposed on the estate. The estate of a U.S. citizen or resident is taxed under the rates contained in Code section 2001(c). These rates range from 18 percent for taxable estates of less than \$10,000 to 55 percent for taxable estates over \$3 million. However, the estates of nonresident aliens who died in 1986 are subject to significantly lower estate tax rates under Code section 2101(d) [24].

Two significant differences exist with respect to deductions. The estate of a U.S. citizen or resident is entitled to a marital deduction for all property transferred to the surviving spouse [25]. The estate of a nonresident alien who died in 1986 is generally not entitled to a marital deduction, except as provided for in several estate tax treaties. Also, the estate of a U.S. citizen or resident can deduct virtually all charitable contributions, whereas the estate of a nonresident alien can only deduct certain contributions [26].

A final difference involves allowable credits. The estate of a U.S. citizen or resident is entitled to a unified credit of \$192,800. This credit effectively exempts from tax a taxable estate with less than \$600,000 of assets [27]. As previously mentioned, the estate of nonresident aliens who died in 1986 is entitled to a unified credit of \$3,600.

which effectively exempts estates from estate taxation if taxable estate is less than \$60,000. Also, the credits for State death taxes, gift taxes, and taxes on prior transfers allowed to the estates of nonresident aliens are subject to special limitations [28].

**DATA ANALYSIS**

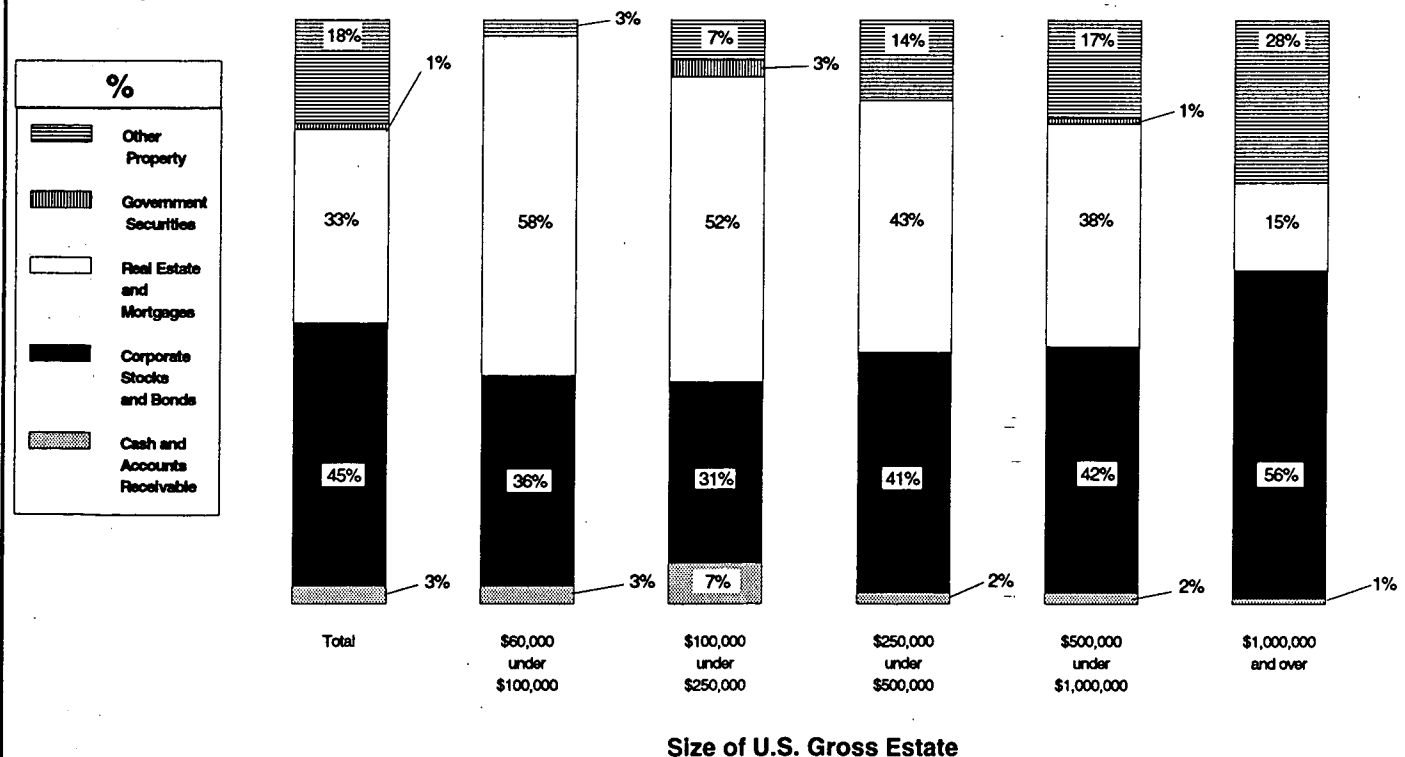
Estate tax returns were filed for the estates of 161 nonresident alien decedents who died during 1986. Total gross U.S. estate of \$62,017,417 was reported for these decedents. The average gross U.S. estate was \$385,201, an increase of 38.1 percent from 1982, the last previous year for which data are available.

Of the 161 returns filed, 89 returns showed the foreign component of gross estate, 55.3 percent of the total number of returns. Gross foreign estate had to be reported only if deductions attributable to gross worldwide estate were allocated to gross U.S. estate. These 89 returns showed total gross U.S. estate of \$41,390,447 and total gross worldwide estate of \$218,983,544. Total gross foreign estate was thus \$177,593,097, which was 76.0 percent greater than 1982 [29].

Stocks and bonds, and real estate and mortgages, constituted the largest categories of property in gross U.S. estate. Together these two categories comprised 78.2 percent of total U.S. property reported. The total value of corporate stocks and bonds reported for the estates of nonresident aliens was \$27,770,401. This amount was a 34.4 percent increase over 1982. Real estate and mortgages equaled \$20,709,960, up 4.1 percent from 1982. However, the greatest increase was for "other property," which was reported as \$11,418,566, nearly triple the amount reported for 1982 [30].

As indicated in Figure B, the relative composition of U.S. assets changed with the size of gross estate. In general, the larger the estate, the greater the proportion of stocks and bonds and other property, and the smaller the proportion of real estate and mortgages. With respect to the smallest estates (i.e., those with assets between \$60,000 and \$100,000), real estate constituted 58.2 percent of U.S. assets, stocks and bonds, 35.6 percent, and other property, 3.0 percent. For the largest estates (i.e., those with assets of \$1 million or more), real estate was only 14.8 percent of U.S. property, whereas stocks and bonds constituted 55.7 percent, and other property, 28.1 percent.

**Figure B**  
**Composition of U.S. Gross Estates, by Size of Estate, 1986**  
**(Percentage of U.S. Gross Estate)**



With respect to individual countries, the largest number of returns were filed for the estates of Canadian decedents. Estate tax returns were filed for the estates of 51 Canadian decedents. These returns comprised nearly one-third of the total number of returns filed. However, many of these returns were filed for relatively small estates. The average gross U.S. estate for returns of Canadian decedents was only \$219,506. Furthermore, these returns accounted for only 18.1 percent of the total U.S. property reported for nonresident alien estates. United Kingdom (U.K.) decedents also had relatively small estates. Although 7.5 percent of the returns were filed for the estates of U.K. decedents, the average estate size was only \$180,647. U.K. returns accounted for only 3.5 percent of the total U.S. property. On the other hand, the estates of West German and Venezuelan decedents were substantially larger than average. About 6.8 percent of the returns were filed for the estates of West German decedents. These estates had an average size of \$659,718 and accounted for nearly 11.7 percent of total U.S. property. In addition, although only 5.0 percent of the returns were filed for the estates of Venezuelan decedents, these estates had an average size of \$1,740,669 and accounted for 22.5 percent of total U.S. property. However, if the returns filed for the few wealthiest decedents are excluded, the average estate size of Venezuelan decedents was substantially lower.

Expenses of \$21,071,425 were reported for the estates of nonresident aliens. This amount was about \$4 million less than 1982. Of this total, \$6,119,675 were deducted from gross U.S. estate [31]. The combined amount for charitable and marital deductions was \$1,889,995, an increase of 746.8 percent from 1982. This increase appeared to be mainly due to the marital deduction. Ten returns showed marital deductions totalling \$1,858,528 [32].

Total taxable U.S. estate was \$53,933,747, an increase of 30.3 percent over 1982. The gross estate tax was \$8,054,638, so that the average tax rate was 14.9 percent. Credits of \$1,534,235 against the gross estate tax were claimed for the estates of nonresident aliens. The largest credit claimed was for State death taxes, \$849,956. This amount represented a 169.0 percent increase from 1982. The second largest credit was the unified credit, \$613,897, a decrease of 1.4 percent from 1982. After credits, the tax liability of the estates of nonresident aliens was \$6,520,403, an increase of 69.4 percent over 1982.

## SUMMARY

The taxable estates of nonresident alien decedents are generally subject to U.S. estate tax on that property

located within the United States. Taxable estate is determined by reducing gross estate by allowable deductions. The estate tax can be reduced by several credits.

Estate tax returns were filed for 161 nonresident alien decedents who died during 1986. Property located within the United States accounted for \$62,017,417 of the worldwide estate of these decedents. The largest categories of U.S. property were stocks and bonds, and real estate and mortgages, which accounted for 44.8 percent and 33.4 percent, respectively, of gross U.S. estate. Taxable estate totaled \$53,933,747, and the gross estate tax equaled \$8,054,638. After taking credits of \$1,534,235, the estates of nonresident aliens faced a U.S. estate tax of \$6,520,403.

## DATA SOURCES AND LIMITATIONS

The data contained in this article and the following table were reported on all Forms 706NA, *United States Estate Tax Return, Estate of nonresident not a citizen of the United States*, filed at the IRS Philadelphia Service Center between January 1986, and October 1988, by personal representatives of the decedents reporting a date of death during 1986. No sampling errors exist since the entire population was included in the study. However, the data contained here do not include information reported on returns with a taxable estate of less than \$60,000, returns showing assets exempt from U.S. estate taxation under the provisions of an applicable estate tax treaty, and returns that were erroneously filed.

The personal representative of the estate had 9 months following the decedent's death to file the return. A 6-month extension could be requested. However, possible delinquencies may have occurred. Therefore, the population may be slightly understated.

One potential data limitation should be mentioned. Seventy-three returns did not report any foreign assets. Therefore, the amounts shown in Table 1 for gross foreign estate and gross worldwide estate do not include the foreign assets for all nonresident alien estates.

## DEFINITIONS OF SELECTED TERMS

*Domicile*.—Domicile is the place where an individual's permanent home is located and from which the individual has no present intention of moving.

*Gross estate*.—Gross estate includes all interests in property that were owned by the decedent at the time of death, that were subject to a power of acquisition at the time of the decedent's death, that were transferred during

the decedent's lifetime in a manner substantially equivalent to a transfer under a will, or that were passed to the decedent tax-free through the use of the marital deduction. Gross worldwide estate includes all property included in gross estate no matter where it is located. However, the foreign component of gross worldwide estate had to be reported only if deductions had to be allocated between the foreign and U.S. estate. Gross U.S. estate includes only that portion of gross estate located within the United States.

*Personal representative.*—A personal representative is an executor or administrator of an estate.

*Taxable estate.*—Taxable estate is the value of the decedent's interests in property net of allowable deductions.

## NOTES AND REFERENCES

- [1] Treasury Regulation section 20.0-1(b). Residency for estate tax purposes differs from residency for income tax purposes. Under Internal Revenue Code section 7701(b), a resident for income tax purposes is an individual who meets the requirements of either the lawful permanent resident test or the substantial presence test. For additional information about residency requirements for income tax purposes, see, for example, Kaplan, Richard L., *Federal Taxation of International Transactions*, West Publishing Company, 1988, pp. 529-35.
- [2] For additional information about the factors considered in determining domicile, see, for example, Oliver, Harry Gordon, "Estate and Gift Tax Planning for Nonresidents," *International Tax Journal*, Fall 1986, p. 300; and Schuldenfrei, A. Finley, Stark, Elwood V. and Cline, Judith Hankins, "Estate Planning Considerations for Nonresident Aliens," *The Tax Adviser*, November 1985, p. 695.
- [3] Revenue Ruling 80-209, *1980-2 Cumulative Bulletin* 248, U.S. Internal Revenue Service, 1980.
- [4] See, for example, *Estate and Gift Tax Treaty Between the United Kingdom and the United States*, Article 4.
- [5] Special rules apply to the taxation of expatriates and residents of U.S. possessions. Under Code section 2107, an expatriate is a U.S. citizen who has lost citizenship within 10 years of death if a principal purpose for the loss of citizenship was the avoidance of U.S. tax. If a nonresident alien is an expatriate, then the alien's estate is taxed under the tax rates that apply to U.S. citizens and residents. Also, the estate of an expatriate must include in gross U.S. estate the value of the assets of a foreign corporation if the decedent owned (directly or indirectly) 10 percent or more of the voting stock of the corporation, or owned (directly, indirectly, or constructively) at least 50 percent of the total combined voting power of all stock of the corporation. For additional information about these special rules, see, for example, Schuldenfrei, Stark and Cline, *op. cit.*, note 2 on p. 703. In addition, under Code section 2107(c), an expatriate is allowed a unified credit of up to \$13,000. Under Code section 2209, a U.S. citizen residing in a U.S. possession is considered to be a nonresident (and is taxed as such) if the individual acquired U.S. citizenship solely by reason of being a citizen of a U.S. possession, or by birth or residency within a U.S. possession. All other residents of U.S. possessions are treated as citizens of the United States.
- [6] Gross estate includes all property, real or personal, tangible or intangible, that was owned by the decedent at the time of death, that was subject to a power of acquisition at the time of the decedent's death, that was transferred during the decedent's lifetime in a manner substantially equivalent to a transfer under a will, or that was passed to the decedent tax-free through the use of the marital deduction.
- [7] Treasury Regulation section 20.2104-1(a).
- [8] Schuldenfrei, Stark and Cline, *op. cit.*, note 2 on p.700.
- [9] Conversely, the stock of a foreign corporation is generally considered to be property located outside the United States. However, in certain cases, U.S. property owned by a foreign corporation controlled by the nonresident alien may be included in the nonresident alien's gross U.S. estate. For more information about this inclusion of property in the nonresident alien's estate, see, for example, Oliver, *op. cit.*, note 2 on p. 300.
- [10] Code sections 2035-2038 require the inclusion in gross estate of certain property transferred by the decedent with restrictions prior to death. Code

section 2035 requires the inclusion in gross estate of property transferred by the decedent within 3 years of the decedent's death. Code section 2036 requires the inclusion in gross estate of transferred property in which the decedent has either retained the right to possess or enjoy the property, or the power to designate who shall possess or enjoy the property. Code section 2037 requires the inclusion in gross estate of property in which the decedent retained an express reversionary interest that another person can possess or enjoy only by surviving the decedent. Code section 2038 requires the inclusion in gross estate of property transferred by the decedent in which the decedent retained the power to alter, amend, revoke or terminate the transfer.

[11] A U.S. person is a citizen or resident of the United States, a domestic corporation or partnership, and an estate or trust that is not considered under the Internal Revenue Code to be a foreign estate or trust.

[12] Code section 2104 does not apply to a debt obligation if Code section 2105(b) (relating to certain debt obligations considered to be property located outside the United States) applies, or if any interest on the obligation would be treated as income from sources outside the United States under Code section 861(a)(1)(B) (relating to interest from a domestic corporation with less than 20 percent of its gross income over a 3 year period from within the United States), Code section 861(a)(1)(G) (relating to interest on certain foreign debt obligations acquired before July 1, 1974), and Code section 861(a)(1)(H) (relating to interest on certain debt obligations of foreign obligors that are guaranteed by a U.S. person).

[13] The debt obligations considered to be located outside the United States include (1) amounts described in Code section 861(c) (i.e., certain deposits with banks, and savings and loan associations, and amounts held by an insurance company under an agreement to pay interest on the amounts), if the interest on the amounts would be treated under Code section 861(a)(1)(A) as income from sources outside the United States (i.e., interest income not effectively connected with a trade or business within the United States that is deposited in a domestic bank or a U.S. branch of a foreign bank); (2) deposits in a foreign branch of a domestic bank; and (3) debt obligations, if the interest on the obligation were exempt from tax under Code sec-

tion 871(h)(1) (relating to the exemption for portfolio interest from the tax imposed on the income of nonresident aliens not connected with a U.S. business).

[14] In addition to these general and specific situs rules, the location of property may be affected by the provisions of an estate tax treaty.

[15] Code section 2106.

[16] In addition, deductions are limited to the amount of property included in gross U.S. estate.

[17] For example, if gross U.S. estate equals \$1 million, gross worldwide estate equals \$2 million, and expenses under Code sections 2053 and 2054 equal \$500,000, then the allowable deduction under Code section 2106(a)(1) equals:  

$$(\$1 \text{ million} / \$2 \text{ million}) \times \$500,000 = \$250,000.$$

[18] A marital deduction may be allowed the estate of a nonresident alien under an applicable tax treaty. For example, Article 8 of the *Estate and Gift Tax Treaty Between the United Kingdom and the United States* allows a marital deduction (to the extent it is allowed to a U.S.-domiciled decedent) for transfers of U.S. property by a U.K.-domiciled decedent to the decedent's spouse.

[19] Adjusted taxable gifts is the total amount of taxable gifts made by the decedent after December 31, 1976, except for gifts otherwise included in the decedent's gross estate. Adjusted taxable gifts is included in the estate tax calculation in order to prevent taxpayers from avoiding the impact of the progressive estate tax rates by making pre-death gifts.

[20] Code section 2102(c). Estate tax returns were not required if taxable estate was less than \$60,000. Therefore, these estates are not included in the statistics.

[21] Two limitations are imposed on the credit that the estate of a nonresident alien can take for State death taxes. Under Code section 2011(b), the credit is limited to a certain percentage of "adjusted taxable estate." In addition, under Code section 2102(b), the State death tax credit is limited to a percentage determined by dividing the value of

property on which the State tax is imposed by the nonresident alien's gross U.S. estate.

- [22] This credit applies only to gifts made before 1977 of property that was subject to gift taxation and which is included in the decedent's gross U.S. estate. With the unification of the estate and gift tax systems by the Tax Reform Act of 1976, the credit is no longer necessary.
- [23] Code sections 2031, 2103.
- [24] In 1988, Code section 2102 was amended so that the rates imposed on U.S. persons under Code section 2001 apply to the estates of nonresident aliens who died after November 10, 1988.
- [25] Code section 2056. There are a number of limitations on the deduction where the interest passing to the surviving spouse is a terminable interest.
- [26] Code sections 2055, 2106(a)(2).
- [27] Code section 2010.
- [28] Code section 2102.
- [29] Gross foreign estate, as well as gross worldwide estate, may be underreported since only 89 returns reported an amount for foreign gross estate.
- [30] As used in this article, "other property" includes all property other than cash and accounts receivable, corporate stocks and bonds, real estate and mortgages, and government securities.
- [31] Expenses were reported on the 89 returns that reported gross foreign estate and by 13 returns which only reported U.S. assets. This latter group showed deductions of \$519,527.
- [32] The amount for the charitable and marital deductions are combined on the Form 706NA, *United States Estate Tax Return, Estate of nonresident not a citizen of the United States*. However, ten returns, accounting for the bulk of the combined charitable and marital deductions had an attached schedule indicating the amount of the marital deduction.

Table 1.—Gross U.S. and Worldwide Estates, Deductions, Taxable Estate, Estate Tax and Credits, by Selected Country of Domicile of Decedent and Size of Gross U.S. Estate

(Money amounts are in full U.S. dollars)

Table with columns: Selected countries and size of gross U.S. estate, Number of returns, Worldwide estate, Estate outside the United States, Total, Cash and accounts receivable, Corporate stocks and bonds, Real estate and mortgages, Government securities, Other property, Funeral and other expenses, Deductions, U.S. taxable estate, Gross estate tax, Credits, U.S. estate tax after credits.

1 These amounts may be underreported since only 89 returns reported an amount for "Estate outside the United States." An estate was required to report this amount only if it allocated deductions for its worldwide estate to its U.S. estate. When this amount was not reported, U.S. estate and worldwide estate would be equal.
2 Includes personal property.
3 Includes U.S. possessions, except Puerto Rico.
Note: Detail may not add to totals because of rounding.