

The Estate Planning Advisor

Planning For a Non-Citizen Spouse

By Richard J. Shapiro, J.D.

Many married couples are familiar with the idea that, upon their death, they can leave unlimited amounts of assets to a surviving spouse without those assets being subject to Federal or State estate taxes. A common estate planning technique is to pass assets of the first spouse to die into a "Family Trust" in a sum up to the current estate tax exemption amount (currently \$2,000,000), with the balance being passed to the surviving spouse, either outright or in a "Marital Trust." In this scenario, upon the surviving spouse's death only those assets that were passed directly to the surviving spouse, or into a Marital Trust for the surviving spouse's benefit, are subject to estate taxes.

These rules, however, do not apply where the surviving spouse is not a United States Citizen. In 1988, Congress passed legislation to remedy what it perceived was an abuse of the tax system. The perception was that many non-citizen spouses were, after the death of the citizen spouse, returning to their homelands and avoiding the United States estate tax system. The 1988 legislation eliminated the Unlimited Marital Deduction for property in excess of \$100,000 where the property passed from a U.S. citizen to a non-citizen spouse. This rule can have a drastic impact on the surviving spouse, often forcing a liquidation of assets in order to pay the estate taxes due within nine months after the death of the citizen spouse.

One ready solution to this problem is to implement an estate planning device called a Qualified Domestic Trust ("QDOT"). So long as the technical requirements are satisfied, use of a QDOT permits assets to pass into a trust for the surviving non-citizen spouse in a manner that will allow that spouse to utilize the Unlimited Marital Deduction. In its basic form, a QDOT allows for distributions of income to the surviving spouse (and distributions of principal on account of "hardship") without being subject to estate tax. Distributions of principal from the QDOT to the surviving spouse (other than hardship distributions) are subject to estate taxes calculated at the marginal estate tax rate of the deceased spouse's estate.

A QDOT may be established as part of the estate plan of the deceased spouse, or even by the surviving spouse so long as the QDOT is formed by the time an estate tax return must be filed (ordinarily nine months after the first spouse's death, but often extended to fifteen months).

Some of the key requirements of a QDOT are (1) at least one Trustee must be an individual U.S. Citizen or U.S. corporation; (2) the U.S. Trustee must be able to withhold taxes due on distributions of trust principal; and (3) the Executor or Trustee of the

deceased spouse's estate must make a QDOT election to qualify the QDOT for the Unlimited Marital Deduction.

Planning for non-citizen spouses is fraught with potential pitfalls. Couples presented with this situation should seek experienced professional advice to avoid the unintended consequences of improper planning, and to take advantage of the available planning opportunities.

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