Tax Planning for Non-U.S. Individuals May Be Thwarted by Recent Tax Reform

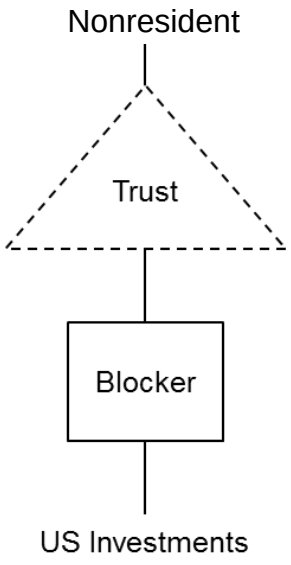
April 2018

A change in the recent tax reform legislation may have important consequence for nonresident alien individuals ("Nonresidents") who have engaged in U.S. estate tax planning and/or who have substantial U.S. investments. Specifically, H.R. 1, enacted on December 22, 2017 (the "Act"), changed the rules for determining when a foreign corporation will be considered a controlled foreign corporation ("CFC") and, in so doing, undermined the utility of foreign "corporate blockers" in U.S. estate tax planning in certain situations.

Nonresidents who rely on foreign corporate blockers need to review their estate planning in light of the new rules. With proper planning, it may be possible to mitigate and/or avoid the impact of the new rules.

Pre-Tax Reform Blocker Structure

A common estate planning technique for Nonresidents who wish to benefit U.S. family members is to hold U.S. assets (including stock in U.S. corporations) through a foreign (i.e., non-U.S.) corporation.



The foreign corporation acts as a blocker which shields the foreign estate from U.S. estate tax liability – i.e., shares in foreign corporations are non-U.S. situs assets and, accordingly, are not included in a decedent's taxable U.S. estate.

Under the prior CFC rules, the trust was able to liquidate the blocker and receive a stepped-up fair market value tax basis in the blocker's assets without incurring any U.S. income tax liability. This was done by causing the blocker to make a "check the box" election to be classified as a disregarded entity within 30 days of the nonresident's death.

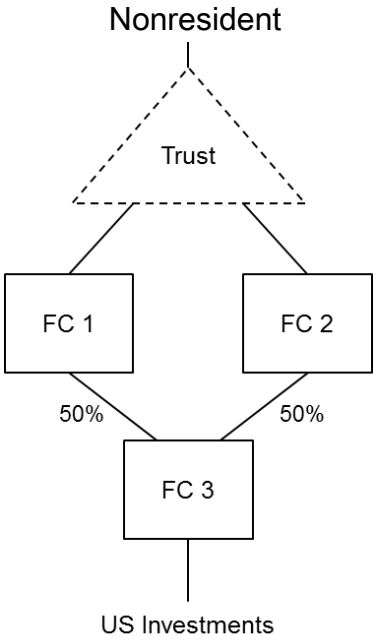
The Act eliminated the 30-day grace period. Thus, under the new rules, the blocker may become a CFC upon the death of the nonresident if U.S. beneficiaries are involved, in which case the blocker cannot be eliminated without potential gain recognition under the CFC rules.

Post Tax-Reform Planning

Nonresidents who have implemented or rely on a blocker structure should consider alternative estate planning and management strategies.

Among other possibilities, one alternative is to establish a triple blocker structure. Under this structure, the trust would directly own two foreign corporations ("FC 1" and "FC 2") which each own 50% of a third foreign corporation ("FC 3") which, in turn owns the U.S. assets.

Following the grantor's death, FC 3 would make a "check the box" election to be treated as a partnership retroactive to before the date of death. FC 1 and FC 2 would then make "check the box" elections to be treated as disregarded entities effective shortly after the grantor's death. This is effective after the date of death so that there would be no U.S. assets on the date of death, and thus no U.S. estate tax. Depending on when in a given year the grantor dies, this structure could permit the trust to eliminate all three companies and receive a stepped-up tax basis in FC 3's assets while incurring little or no income tax liability.



The choice of the optimal structure will depend on the Nonresident's unique facts and circumstances. Nonresidents who wish to benefit U.S. family members and have substantial U.S. investments may contact any one of the attorneys listed below to discuss how the changes under the Act will affect their estate tax planning.

* * * * *

About Curtis

Curtis, Mallet-Prevost, Colt & Mosle LLP is a leading international law firm. Headquartered in New York, Curtis has 17 offices in the United States, Latin America, Europe, the Middle East and Asia. Curtis represents a wide range of clients, including multinational corporations and financial institutions, governments and state-owned companies, money managers, sovereign wealth funds, family-owned businesses, individuals and entrepreneurs.

For more information about Curtis, please visit www.curtis.com.

Attorney advertising - the material contained in this news alert is only a general review of the subjects covered and does not constitute legal advice. No legal or business decision should be based on its contents.

Please feel free to contact any of the persons listed below if you have any questions on this important development:

Marco Blanco
Co-chair, Partner
Tax Practice
Private Client Practice
mblanco@curtis.com
Geneva: +41 22 718 3518
Paris: +33 1 42 68 72 00

Klas Holm
Co-chair, Partner
Tax Practice
Private Client Practice
kholm@curtis.com
New York: +1 212 696 8800

Eduardo Cukier
Partner
Tax Practice
Private Client Practice
ecukier@curtis.com
New York: +1 212 696 6107

Robert Sheehan
Chair, Partner
Private Client Practice
Trusts and Estates Practice
rsheehan@curtis.com
New York: +1 212 696 6176

Michael S. Schwartz
Partner
Private Client Practice
Trusts and Estates Practice
michael.schwartz@curtis.com
New York: +1 212 696 8823