

# Basis Step-up Techniques for Gifts to US Persons

STEP – TEL AVIV

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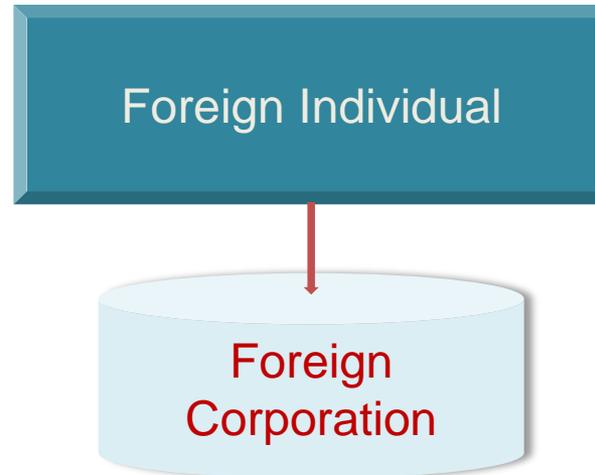
# Fact Pattern 1

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Lior is not a citizen and is not domiciled in the United States. Lior has \$11 million of US assets that he desires to leave to US persons on his death. Lior had been previously advised that he should form a non-US holding company to hold US assets which might eventually be inherited by US persons and currently has this ownership structure in place.

# Foreign Company Holding Structure under Prior Law

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1. Immediately after death of foreign individual, foreign corporation would “check the box” to be taxed as a disregarded entity.
2. This was a deemed liquidation under US law.
3. At death, foreign shareholder did not own any US assets, so there was no estate tax exposure.
4. Under pre-2018 law, a foreign corporation was not a “controlled foreign corporation” (“CFC”) unless US shareholders held shares in the CFC for more than 30 days during the taxable year.
5. Because of the immediate liquidation following the death of the foreign individual US persons did not own stock of the CFC for more than 30 days. Accordingly, the Foreign Corporation was not a CFC.

# Analysis under the New Controlled Foreign Corporation Rules

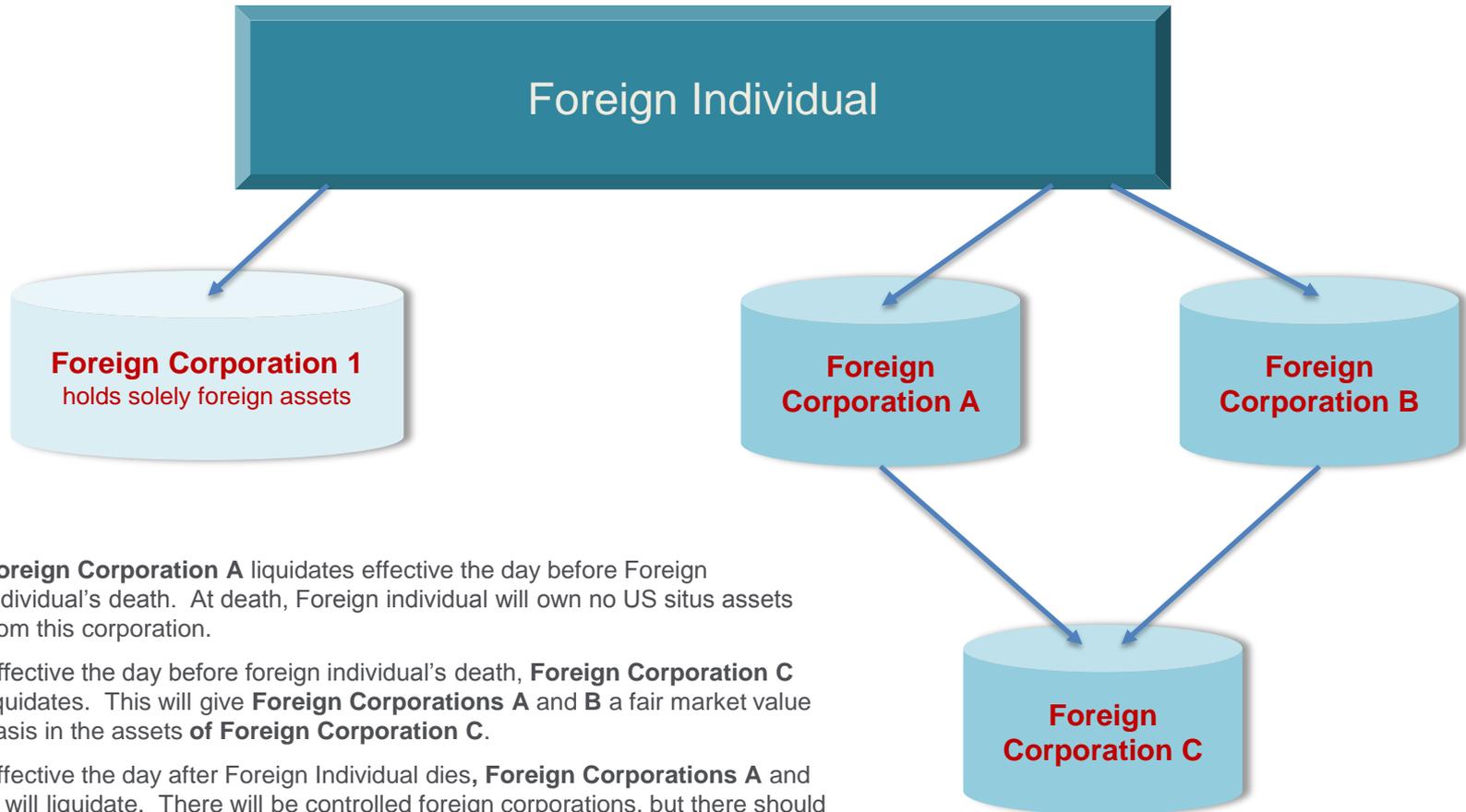
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1. Under post-2017 law, a foreign corporation can be a controlled foreign corporation if US shareholders own stock in the CFC for even a second.
2. The deemed liquidation of a CFC following 2017 will result in gain at the corporate level, which would flow through to the shareholders under the CFC rules.
3. On the deemed liquidation, the US shareholders would get a capital loss, but this loss would be limited in its ability to offset the CFC gain flowing through.
4. **Foreign individuals who relied on this planning technique need to revisit their planning immediately.**



# Two Tiered Holding Company Structure

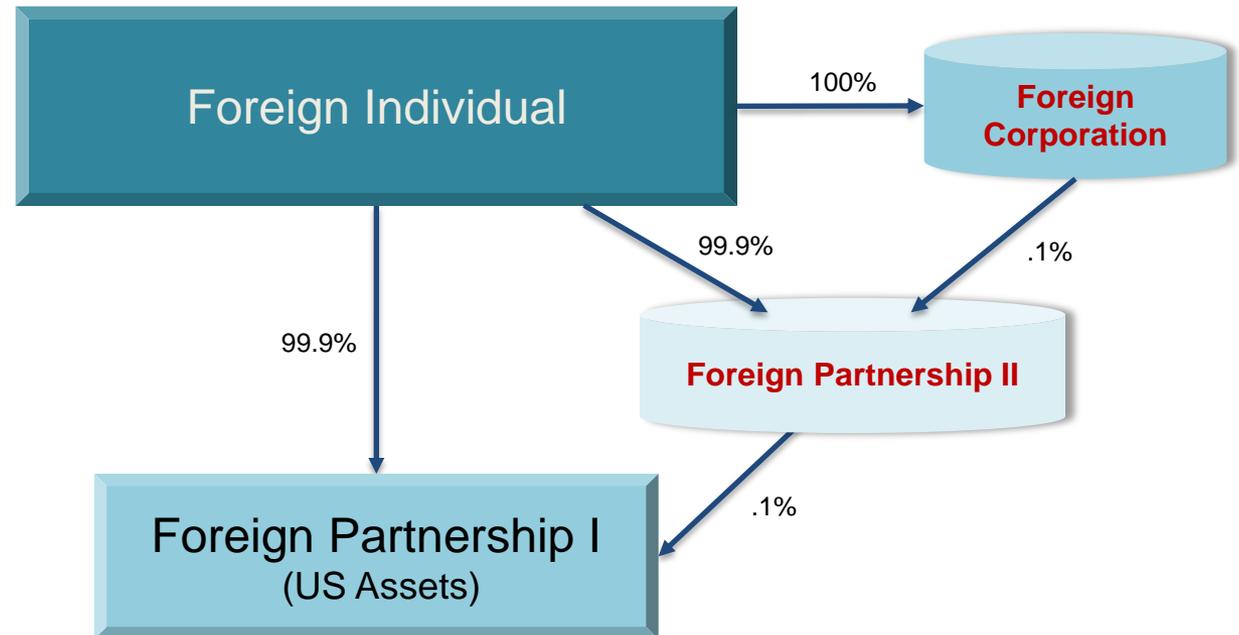
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1. **Foreign Corporation A** liquidates effective the day before Foreign Individual's death. At death, Foreign individual will own no US situs assets from this corporation.
2. Effective the day before foreign individual's death, **Foreign Corporation C** liquidates. This will give **Foreign Corporations A** and **B** a fair market value basis in the assets of **Foreign Corporation C**.
3. Effective the day after Foreign Individual dies, **Foreign Corporations A** and **B** will liquidate. There will be controlled foreign corporations, but there should be minimal gain on the liquidation.
4. Potential concerns include added cost, Internal Revenue Code Section 269.

# Two Tier Partnership Structure

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1. Taxpayer takes position that an interest in foreign partnership holding US assets is not US situs property.
2. Effective immediately after death of foreign individual, liquidation of foreign partnership.
3. Continued viability of this this technique is uncertain following the repeal of the *Grecian Magnesite* case.

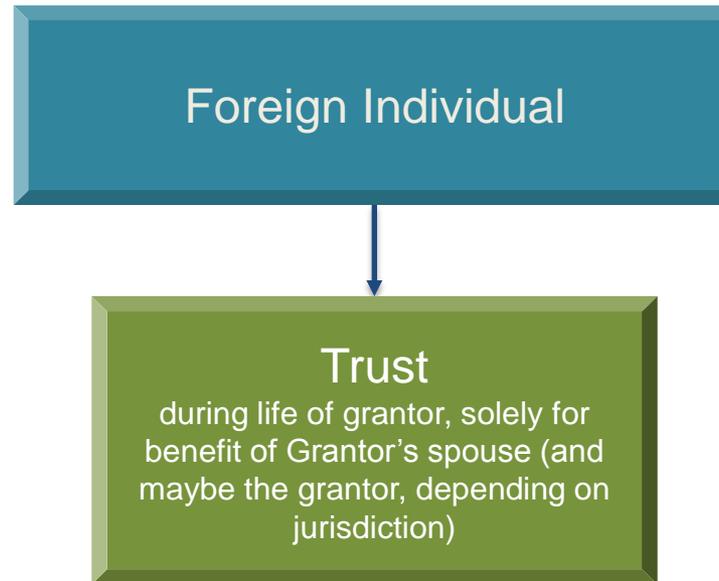
# Tax Gain Harvesting

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1. US Tax rules prohibit selling stock at a loss, rebuying it within thirty days, and taking the tax loss.
2. No corresponding rule applies to selling a stock at a gain and rebuying it immediately. This technique, if applied frequently could leave a foreign holding company holding US stocks with no positions which would trigger gains on a deemed post-death liquidation.
3. IRS might argue lack of economic substance.
4. Thus, best to repurchase similar, but not identical securities, and to wait 31 days before rebuying the same security.

# Grantor Trust Structures

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1. For US trusts, the assets in the trust receive a basis step-up at death only if the assets are includable in the estate of the grantor.
2. This defeats the purpose of holding US assets in an irrevocable trust.
3. Under PLR 201245006, assets in a trust which is a grantor trust to a foreign grantor can receive a basis step-up even if the assets are not includable in the estate of the grantor.
4. Grantor might be able to be a beneficiary of the trust and not have assets included in the estate. If the trust is formed in certain asset protection jurisdictions (including Delaware, Atlanta, the Bahamas).

## Fact Pattern 2

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In 2013, Husband and Wife were each worth \$5 million. Husband transferred \$5 million of assets, having a tax tax basis of \$5 million, to an irrevocable dynasty trust. In 2018, the Trust and wife each hold assets worth \$10 million, with a basis of \$5 million. Is there any way for the trust to step up the basis of its assets to fair market value?

# General Power of Appointment

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1. Assets will receive a basis step-up to fair market value if they are includable in the estate of a person on that person's death.
2. If a person holds a general power of appointment over assets held by a trust, the assets are includable in that person's estate. A general power of appointment includes the ability to direct a trustee to distribute assets to a person himself, his creditors, his estate or creditors or his estate.
3. If the assets over which the power of appointment is held are non-US, the holding of the power should not create any adverse US estate tax consequences. Query whether the holding of a power of appointment by an Israeli taxpayer could produce adverse Israel tax consequences.
4. If the assets over which the power is held are US, a US person should hold this power in order to take advantage of the \$11.2 million estate tax exemption.
5. This technique, makes it worthwhile to search for elderly, poorer US relatives.