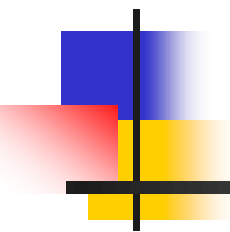


# **CROSS-BORDER TAXATION OF ESTATES**

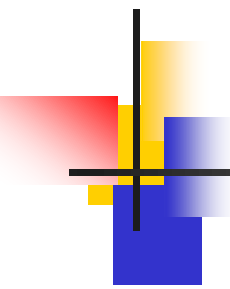
## **CASE STUDIES**



---

**by: Mr. Paresh P. Shah**

P.P. Shah & Associates  
Chartered Accountants  
Email: [ppshahandassociates.com](mailto:ppshahandassociates.com)

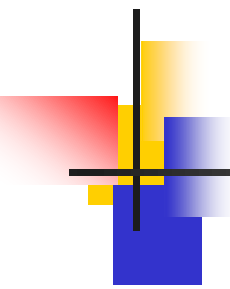


# CASE-STUDY 1: INDIAN GRANTOR TRUST WITH U.S. BENEFICIARIES

---

## FACTS OF THE CASE:

- Mr. 'X' is a tax resident of U.S. and is living with his wife and three children in the U.S.
- Mr. 'A', an Indian citizen and resident, is the father of Mr. 'X'
- Mr. 'A' desires to gift his immovable properties located in India to his son Mr. 'X'
- However, income from such immovable properties shall be taxable in the hands of Mr. 'X' both in U.S. and in India
- Further, on death of Mr. 'X', the properties shall form part of his estate and shall be subject to Estate tax in U.S.
- Mr. 'X' has approached KNAV for their expert advice



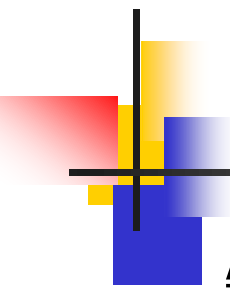
## CASE-STUDY 1: (con't)

### INDIAN GRANTOR TRUST WITH U.S. BENEFICIARIES

---

#### KNAV'S ADVICE & SOLUTION:

- Mr. 'A' to settle the immovable properties located in India on to an Indian trust for the benefit of his son Mr. 'X', his daughter-in-law and his three grand-children
- The Indian Trust should be in the nature of a Grantor Trust as defined under U.S. tax codes
- Mr. 'A', the settlor, should retain the right to revoke the settlement in order to qualify as Grantor Trust



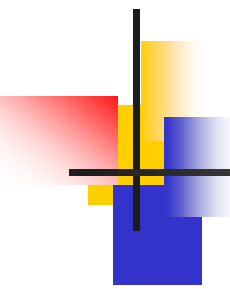
## CASE-STUDY 1: (con't)

# INDIAN GRANTOR TRUST WITH U.S. BENEFICIARIES

### Analysis & Discussions:

#### Grantor Trust: US Tax implications

- An Indian / foreign (i.e. non-U.S.) trust is not subject to U.S. income tax except for withholding tax on any U.S. source income.
- However, distributions from the foreign trust to a U.S. person (a U.S. citizen or a U.S. resident) will carry out distributable net income to that person, with adverse tax treatment of accumulated income, unless the trust qualifies as a "Grantor Trust" under U.S. law.
- If trust qualifies as Grantor Trust, the U.S. beneficiary pays no tax on the income distributed to him from the trust (although he must report the income to the IRS).
- Therefore, a U.S. beneficiary of a foreign trust will greatly prefer that the trust be a Grantor Trust with a non-U.S. person as grantor.



## CASE-STUDY 1: (con't)

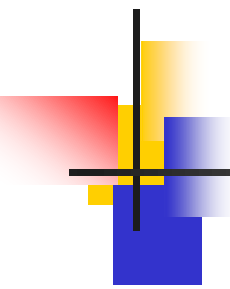
# INDIAN GRANTOR TRUST WITH U.S. BENEFICIARIES

---

### Analysis & Discussions:

#### Grantor Trust: US Tax implications

- A non-U.S. person will be treated as the grantor of a trust only if one of the following requirements is met:
  - If the Grantor has the full power to revoke the trust without the consent of any person, or with the consent of a subservient third party
  - If the Grantor (and, if desired, the Grantor's spouse) are the sole beneficiaries of the trust during the life of the Grantor
- Once the non-U.S. grantor dies, the offshore trust which previously qualified as a grantor trust under one of the exceptions is no longer a grantor trust, and all income distributed to the U.S. beneficiary will be taxed to him or her.

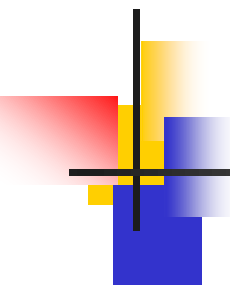


## CASE-STUDY 1: (con't)

### INDIAN GRANTOR TRUST WITH U.S. BENEFICIARIES

#### Tax Implications Of KNAV's Advice & Solution:

- During the life of Mr. 'A', the settlor: (a) all income from the trust assets shall be taxable in his hands in India only, and (b) such income may be accumulated and distributed later without any incidence to tax on the U.S. beneficiaries
- On the death of Mr. 'A', the trust shall become a non-Grantor Trust. It should distribute every year's income (including capital gains) to the U.S. beneficiaries which is taxed to the beneficiary in their hand
- After all current income of the non-Grantor Trust has been carried out to the beneficiaries, further distributions are treated as distributions of corpus and are not taxed (assuming the trust has no accumulated income from prior years after it has become a non-Grantor Trust)

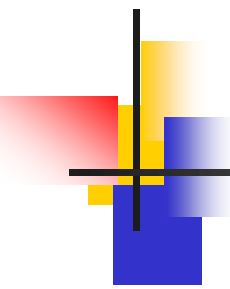


## CASE-STUDY 1: (con't)

# INDIAN GRANTOR TRUST WITH U.S. BENEFICIARIES

### Tax Implications Of KNAV's Advice & Solution:

- However, if current income is accumulated, it suffers tax disadvantage as under:
  - All capital gains realized by the trust in prior years are carried out to the beneficiary, but at ordinary income rates
  - An interest charge is imposed on the tax due by the beneficiary on the accumulated income per annum from the date the income was originally earned by the trust and is compounded daily.
  - The income may be taxed at the beneficiary's tax bracket for the years in which income was accumulated.
- No Estate taxes are payable on death of Mr. 'A', as he was not a U.S. person and the assets are not U.S. situs assets
- Further, also on death of Mr. 'X', the U.S. beneficiary, no Estate taxes are payable on the Indian assets as they are not a part of his estate

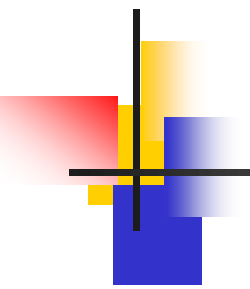


## CASE-STUDY 2: U.S. GRANTOR TRUST WITH INDIAN BENEFICIARIES

---

### FACTS OF THE CASE:

- Mr. 'X' is a tax resident of India and is living with his wife and three children in India
- Mr. 'A', a resident of U.S., is the father of Mr. 'X'
- Mr. 'A' desires to gift his immovable properties located in U.S. to his son Mr. 'X'
- However, income from such immovable properties shall be taxable in the hands of Mr. 'X' both in U.S. and in India
- Further, on death of Mr. 'X', the properties, being U.S. situs assets shall form part of his estate and shall be subject to Estate tax in U.S.
- Mr. 'X' has approached KNAV for their expert advice on tax implications if Grantor Trust is created

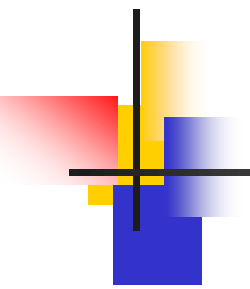


## CASE-STUDY 2: (con't)

### U.S. GRANTOR TRUST WITH INDIAN BENEFICIARIES

#### DISCUSSIONS OF U.S. GRANTOR TRUST:

- As Mr. 'A', the settlor is a tax resident of U.S., and he settles his U.S. situs assets on to a trust, the resultant trust would be a U.S. Trust as it would meet both of the following tests:
  - I. Court Test i.e. a court in U.S. may have primary supervision over the Trust as it has U.S. situs assets, and
  - II. Control Test i.e. one or more U.S. persons (i.e. the trustee/s) would have the authority to control all substantial decisions of the trust
- If Mr. 'A' retains the right to revoke the settlement, the trust would be a U.S. Grantor Trust. All income from the trust assets would be taxable in the hands of the settlor and not the Indian beneficiaries as per U.S. law.
- As the settlement is revocable in nature, under Indian tax laws also, the Indian beneficiaries shall not be taxable on the trust income as provided under Section 61 of the Indian Income-Tax Act, 1961.

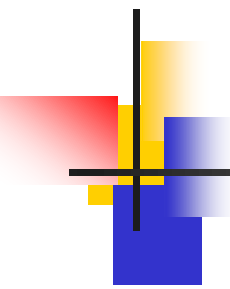


## CASE-STUDY 2: (con't)

### U.S. GRANTOR TRUST WITH INDIAN BENEFICIARIES

#### DISCUSSIONS OF U.S. GRANTOR TRUST:

- On settlement of property to a revocable trust, U.S. Gift Tax liability would not be incurred until the property is transferred to a beneficiary or when the trust becomes irrevocable
- On death of Mr. 'A', the settlor, the trust becomes a non-grantor trust. Accordingly, current income should be distributed to the beneficiaries to avoid incidence of unfavourable tax treatment of accumulated income as per U.S. tax laws
- Further, on death of Mr. 'A', the trust assets, being U.S. situs assets shall be subject to Estate taxes.
- Therefore, for U.S. situs assets, whether they are held in personal name or settled on a trust, U.S. income tax and Gift / Estate taxes on death of settlor would always be applicable.
- After death of Mr. 'A', the trust income shall be taxable both in U.S. and in India (with tax credit). Indian beneficiaries shall be taxed at maximum marginal tax rate as provided under the Indian Income-Tax Act, 1961

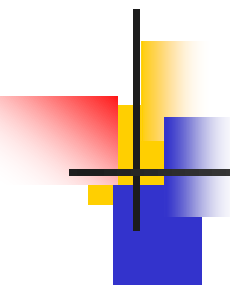


## CASE-STUDY 3: INDIAN TRUST WITH U.K. BENEFICIARIES

---

### FACTS OF THE CASE:

- Mr. 'X' is a tax resident and domicile of U.K. and is living with his wife and three children in the U.K.
- Mr. 'A', an Indian citizen and resident, is the father of Mr. 'X'
- Mr. 'A' desires to gift his immovable properties located in India to his son Mr. 'X'
- However, income from such immovable properties shall be taxable in the hands of Mr. 'X' both in U.K. (U.K. tax resident & domicile is taxed on worldwide income) and in India (as source of income)
- Further, on death of Mr. 'X', the properties shall form part of his estate and shall be subject to Inheritance tax in U.K.
- Mr. 'X' has approached KNAV for their expert advice



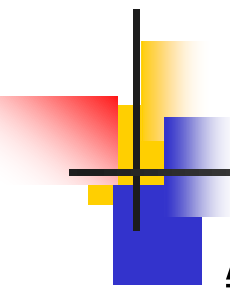
## CASE-STUDY 3: (con't)

### INDIAN TRUST WITH U.K. BENEFICIARIES

---

#### KNAV'S ADVICE & SOLUTION:

- Mr. 'A' to settle the immovable properties located in India on to an Indian trust for the benefit of his son Mr. 'X', his daughter-in-law and his three grand-children
- The Indian Trust would be in the nature of a Non-Resident Trust as per U.K. tax codes
- Non-Resident Trust is usually one where:
  - (i) All the Trustees are non-resident, or
  - (ii) Some of the Trustees are non-resident and the Settlor was non-UK domiciled and non-resident when Trust was set up
- Unlike in U.S., there is no concept of a Grantor or non-Grantor Trust in U.K.



## CASE-STUDY 3: (con't)

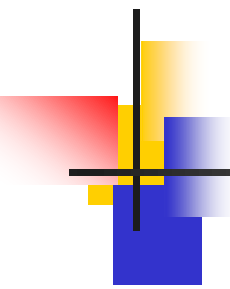
### INDIAN TRUST WITH U.K. BENEFICIARIES

---

#### Analysis & Discussions:

##### Non-Resident Trust: U.K. Tax implications

- An Indian / Non-Resident (i.e. non-U.K.) trust is not subject to U.K. income tax except for tax on any U.K. source income based on the type of trust.
- It would be outside the scope of the UK inheritance tax discretionary trust regime as the trust is an excluded property trust (holds non-UK assets and settlor non-domiciled at the relevant time).
- Thus, Indian situs assets could be considered for settlement to an Indian trust when UK resident / domiciled was a non-domiciled of UK
- If U.K. Resident & domiciled Beneficiary gets income from the non-resident trust, he is subject to tax on the same as world-wide income but can get some tax relief if the trustees have already paid tax on the income.
- However, if beneficiary is U.K. resident but not U.K. domiciled, his foreign income may be taxed on 'remittance basis'



# CASE-STUDY 3: (con't)

## INDIAN TRUST WITH U.K. BENEFICIARIES

---

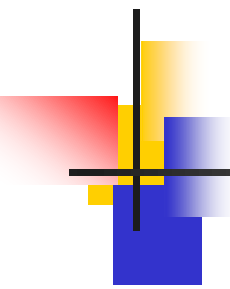
### **DOMICILE STATUS:**

Your domicile status is decided under general law, which means it must be interpreted according to previous rulings of the courts. There are many things which affect your domicile. Some of the main points are:

- you cannot be without a domicile
- you can only have one domicile at a time
- you are normally regarded as domiciled in the country where you have your permanent home
- your existing domicile will continue until you acquire a new one
- your domicile is distinct from your nationality, citizenship and your residence status, although these can have an impact on your domicile

There are three types of domicile:

- domicile of origin (normally that of the father or in case of unwed parents, of mother)
- domicile of choice (settling in another country after attaining legal capacity to acquire new domicile at age of 16)
- domicile of dependence (domicile of the person on whom you are legally dependant)



## CASE-STUDY 3: (con't)

### INDIAN TRUST WITH U.K. BENEFICIARIES

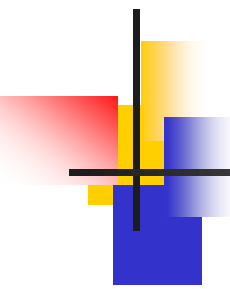
---

- REMITTANCE BASIS:

If a UK-Resident but non-domiciled is not remitting overseas income & gains, he may opt for 'Remittance' basis of taxation by paying (i) GBP 30,000 if he has lived in UK for 7 out of past 10 yrs; (ii) GBP 50,000 if he has lived in UK for 12 out of past 14 years

- DEEMED DOMICILE:

If he is domiciled in UK within previous 3 years or he is tax resident in UK in 17 out of 20 years preceding the death / gift.

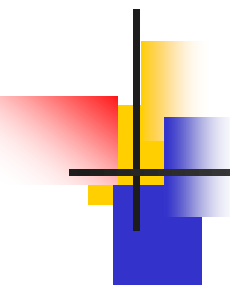


## CASE-STUDY 4: U.K. TRUST WITH INDIAN BENEFICIARIES

---

### FACTS OF THE CASE:

- Mr. 'X' is a tax resident of India and is living with his wife and three children in India
- Mr. 'A', a U.K. resident & domiciled, is the father of Mr. 'X'
- Mr. 'A' desires to gift his immovable properties located in U.K. to his son Mr. 'X'
- However, income from such immovable properties shall be taxable in the hands of Mr. 'X' both in U.K. (as source income) and in India (as resident is taxed on world-wide income)
- Further, on death of Mr. 'X', the properties, being U.K. situs shall form part of his estate and shall be subject to Inheritance tax in U.K.
- Mr. 'X' has approached KNAV for their expert advice



# CASE-STUDY 4: (con't)

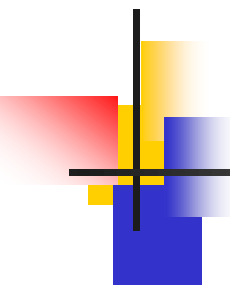
## U.K. TRUST WITH INDIAN BENEFICIARIES

---

### Analysis & Discussions:

#### U.K. Trust: U.K. Tax implications

- Different kinds of trusts in U.K. are taxed differently and have different rates of income-tax. Trustees are generally responsible for paying the taxes.
- If the settlement is revocable in nature, under Indian tax laws, the Indian beneficiaries shall not be taxable on the trust income as provided under Section 61 of the Indian Income-Tax Act, 1961 else they shall be subject to taxes in India in addition to the tax paid by the trust in U.K. (though tax credit would be available in India)



# CASE-STUDY 4: (con't)

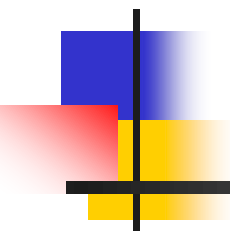
## U.K. TRUST WITH INDIAN BENEFICIARIES

---

### Analysis & Discussions:

U.K. Trust: U.K. Tax implications

- Inheritance Tax:
- UK discretionary Trust: The settlement to a UK discretionary trust would usually be a chargeable lifetime transfer and the trust itself would be subject to the inheritance tax regime for discretionary trusts. As such there would be a 10 year anniversary charge and an exit charge on the distribution of assets from the trust.
- Tax on Settlor on transfer as gift tax only if he does not survive 7 years
- Every 10 years there would be tax on mark-to-market basis and tax on eventual distribution again on mark-to-market basis
- However, if the settlor survives for 7 years from the date of the transfer, the assets transferred would usually be excluded from their estate for inheritance tax purposes. Thus 7 year survival is treated as no 'misuse'



# Thank You

---