

Unpleasant Surprises When a Foreign National Dies Owning Property in New York

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Many foreign nationals own a house or apartment along with other assets in New York (foreign nationals are persons who are not U.S. citizens or residents (or, nonresident aliens)). They are referred to here as “foreigners.”

Unpleasant surprises may be in store for a foreigner’s family and beneficiaries when he/she dies owning real estate, a cooperative apartment, tangible personal property or financial accounts in New York. What steps must the family take to get access to the New York assets? Which country’s law will be applied? Will the estate be required to pay federal estate taxes?

The purpose of this article is to alert practitioners to how easily a foreigner’s New York estate can be compelled to bring a proceeding in a New York Surrogate’s Court and owe federal (and sometimes state) estate taxes, all of which add significant expense and delays before beneficiaries can receive the New York property. Unfortunately, the most vulnerable people are foreigners with small estates who fail to plan for what happens to New York and other U.S. situs assets on their death.

Obviously, planning should be completed during a foreigner’s life to achieve the best outcome for the family and beneficiaries. Without it, here is what can happen.

If Decedent Died Intestate

In general, if a foreigner dies without a will, New York’s law of intestacy will govern what happens to



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New York situs assets. New York’s law of intestacy (EPTL Section 4-1.1) distributes assets by ranking decedent’s surviving relatives and determining who the beneficiaries will be. New York “situs” assets include real estate and tangible personal property such as furniture, cars, art or collectibles held in the decedent’s name in New York at the time of the decedent’s death (a limited liability company [LLC] owned by the decedent that holds New York real estate may not be considered New York situs but will be considered U.S. situs property).

The decedent’s family will have to hire an attorney to bring an ancillary administration proceeding in a New York County Surrogate’s Court to appoint someone with legal authority to access the assets and administer the New York estate (“ancillary” because the New York proceeding generally follows one in the

home country where the process to transfer the foreigner's assets usually begins).

"Non New York situs" assets surprisingly include some assets located in New York such as a personal checking account at a New York bank. New York law does not govern "non situs" assets. Instead, the law of the decedent's domicile governs.

If the Decedent Left a Will

If the decedent had a will and it was submitted to the proper authorities in the home country, it will be necessary to bring an ancillary *probate* proceeding in a New York Surrogate's Court. A foreign will that has been accepted as valid in the decedent's home country will generally be treated as valid to dispose of the decedent's New York situs property. The New York court will require authentication of any documents presented in a foreign court proceeding along with certified translations of those documents if they are not in English.

Who can be named as an ancillary administrator or executor in a New York court proceeding? Generally, the home country is where the family begins this process. The law of the decedent's domicile will determine the legal representative/person empowered to transfer the assets to beneficiaries in the home country. With respect to New York situs property, this person will have first priority to petition the New York Surrogate's Court to be appointed as the ancillary administrator or executor of the New York assets.

However, New York's law governing eligibility to act as ancillary administrator or executor (SCPA Section 707 (1)(c)) disqualifies a foreigner unless a New York resident co-fiduciary is simultaneously appointed. A foreign fiduciary or person with custody of the property in the home country has the alternative of specifying a New York person, bank or financial institution as the sole fiduciary of the New York estate.

'Situs'

Ascertaining an asset's legal or estate tax "situs" is not intuitive. For instance, a checking account at a New York bank is not New York (or U.S.) "situs" property, but a money market account (depending on the underlying assets) held by decedent in the same bank may be considered U.S. situs property. It's frustrating for practitioners and clients if a decedent's only

asset in New York turns out to be a small checking account. New York law does not actually require that an ancillary administrator or executor be appointed, but in practice banks and financial institutions often refuse to give anyone access to a foreign decedent's account until directed to do so by a fiduciary appointed in New York.

So, in practice, the family of a foreign decedent owning certain assets located in New York will usually be compelled to bring a proceeding in the Surrogate's Court to appoint a fiduciary legally qualified to transfer the decedent's assets. In the New York metro area, a proceeding for ancillary administration or probate is often expensive, cumbersome and maddeningly slow. It may take between four months and a year.

Additional Ancillary Proceedings

If real estate, tangible personal property or financial accounts are also held in other states as well as New York, these states may require their own ancillary court proceedings to appoint a fiduciary to manage those assets. This is in addition to the New York proceeding.

'Domicile'

The concept of "domicile" is central to the analysis of what laws and taxes will apply to the decedent's estate. A foreigner may have owned property in multiple countries and spent time in each of them. For federal transfer tax purposes (estate, generation skipping transfer tax and gift tax), the United States defines "domicile" as the place a person lives and intends to return to with no present intention of leaving. Other countries define domicile differently. Therefore, it's possible to have more than one country claiming to be a decedent's domicile at death and attempting to impose its tax regime on the decedent's estate. This situation cries out for advance planning by foreigners with property in multiple countries.

Major Impact of an Estate Tax Treaty with the United States

The United States has estate tax treaties with 15 countries: Australia, Austria, Denmark, France, Germany, Japan, the United Kingdom, Canada, Finland, Greece, Ireland, Italy, the Netherlands, South Africa and

Switzerland. The estate tax treaties help clarify questions of domicile, mitigate double taxation between the treaty countries and provide other benefits not available to decedents from non-treaty countries. Notably absent from the treaty list are China, Israel and all of South America, Central America and Mexico.

If there's no treaty between the foreigner's home country and the United States, the federal estate tax consequence can be enormous. The estate of a foreigner from a non-treaty country can only shelter \$60,000 from federal estate tax versus \$13.61 million that a U.S. citizen or U.S. resident can shelter from estate and gift tax and also from generation skipping transfer tax. The value of the U.S. estate above \$60,000 will be taxed at 40% for federal estate tax purposes. Another significant surprise: there is no marital deduction for transferring assets to a spouse unless the spouse is a U.S. citizen.

If the New York situs assets are valued at over \$6.94 million, New York state will impose its own estate tax as well. In comparison, the federal estate tax, because of the lower \$60,000 exemption amount, can capture even small estates that hold New York real estate or other U.S. situs property.

Estate Tax Analysis Separate From That for Surrogate's Court Proceeding

Determining whether the estate is taxable for estate tax purposes is a separate inquiry from the procedural question of whether an ancillary proceeding must be brought in New York or in any other state. The Treasury Department and New York State will only tax the decedent's U.S. and New York situs assets respectively. U.S. situs property includes stock in U.S. companies, real estate (including cooperative apartments) located in the United States, money market accounts in the United States, funds held in a bank or brokerage account used in conjunction with a U.S. trade or business, and debt instruments privately offered by U.S. organizations (but not publicly traded bonds). A partnership or LLC may or may not be considered U.S. situs depending on the facts and circumstances.

Avoiding a court proceeding in New York, however, will generally have no impact on whether estate taxes are due.

Planning—Avoiding a New York Court Proceeding and Mitigating Estate Taxes

Various planning strategies can avoid ancillary court proceedings and mitigate estate taxes, but there's no "one size fits all" solution. Avoiding a court proceeding in New York will save on court filing fees, legal fees and delays created by court backlogs, all of which delay final distribution of the assets to the beneficiaries and deplete the estate. Revocable trusts, frequently used by New Yorkers and others to avoid a probate or administration proceeding, may work, but not always (such as when decedent is from a civil law country that does not recognize trusts, e.g. France or Italy).

How a New York asset is titled may provide another technique to enable a foreign decedent's estate to skip a New York court proceeding. For example, if New York real estate or a cooperative apartment is held as joint tenants with right of survivorship or tenants by the entirety, the survivor may not need to bring a separate court proceeding in New York to transfer the property.

Similarly, beneficiary designations may work; for example a "transfer on death" or "pay on death" financial account may enable the named beneficiary to skip a New York court proceeding.

Tax mitigation may be possible using complex business structures that seek to change the categorization of the asset as U.S. situs for estate tax purposes.

Conclusion

Attorneys and tax experts specializing in estate planning and cross border tax in both New York and the foreigner's home country may be able to devise a plan to minimize overall expenses and taxes and expedite the process of transferring the assets to the beneficiaries. They should act during the foreigner's life.

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