

MAKING SENSE OF FOUR TRANSATLANTIC ESTATE TAX TREATIES: US-France, US-Germany, US-Netherlands, and US-United Kingdom

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I. Introduction

The purpose of this paper is to present a summary of the principal rules for the allocation of estate taxes and the avoidance of double taxation under four of the most important estate tax treaties to which the United States is a party - the treaties with France, Germany, the Netherlands and the United Kingdom. Each of these treaties follows the “modern” approach to estate tax treaties, where the determination of a decedent’s domicile (rather than the situs of the decedent’s property) is the principal criterion for determining the allocation of taxes and the distribution of related tax credits.

The first part of the paper describes the rules for determining domicile incorporated by these treaties together with a description of the relevant variations contained in specific treaties. The second part of the paper describes the treatment, under ten scenarios, of the allocation of taxes and credits, again with a description of the relevant variations contained in specific treaties. The last section of the paper reviews certain provisions regarding the treatment of property passing to surviving spouses and charities.

II. Domicile

1. Each reference to domicile in a treaty is a reference to domicile as determined under the relevant treaty. While treaty domicile is related to the determination of domicile or residence under the law of the taxing country, the concept of treaty domicile is not necessarily the same as the concept of domicile or resident under national laws.

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2. As a preliminary matter, a person is domiciled in a treaty country if that country considers the person domiciled under its internal transfer tax law.¹

*Exception: Under the US-UK Treaty, a US citizen (“USC”) is considered domiciled in the United States, as a preliminary matter, only if the USC was domiciled in the United States at some point during the three preceding years. This limitation does not preclude the US from worldwide taxation on the basis of citizenship even if the person did not meet this test.*²

3. European countries do not generally tax on the basis of citizenship. Nonetheless, in the case of a person who is a citizen of one country but domiciled in the other country under that other country’s laws, citizenship can be relevant to determine treaty domicile.

(a) For example, under the US-UK Treaty, a USC who is not a UK citizen and who was resident for income tax purposes in the United Kingdom for less than 7 of the preceding 10 years (without regard to the issue of whether the person had a home there) is treated as a US treaty domiciliary. The same rules applies to a UK citizen living in the United States except that the availability of a “dwelling – home” in the US is not excluded from consideration in determining whether the person was a US income tax resident.³

(b) If each country considers a person its domiciliary, under its domestic rules, the following timing rules also apply:

(i) US-Germany: If a person is a citizen of one of the countries but not of the other country, neither person nor member of that person’s family forming part of the household can be considered a domiciliary of the other country until that person has been a domiciliary of the other country for ten years.⁴

(ii) US-France: If a person is citizen of only one of the countries, the other country cannot tax that person on the basis of domicile if that person was present in the other country for less than five out of seven years and

¹ UK4(1), FR4(1), NETH4(1), GER4(1).

² UK4(1)(a), 5(1)(b).

³ UK4(2)&(3).

⁴ GER4(3).

maintained the intent to retain domiciled in the citizenship country. The intent requirement is disregarded if the person was in the other country for employment reasons or was the spouse or other dependent of such a person. The period is extended to less than seven out of ten years if the person was in the other country by renewal of an assignment of employment or as a spouse or dependent of such person.⁵

(iii) US-Netherlands: If a person is a citizen of only one of the countries, the other country cannot tax that person on the basis of domicile if that person was present in that other country for less than seven out of ten years and the person was in the other country for professional, educational, tourism or similar purposes and did not have a “clear intention to remain indefinitely” in the other country.

4. Each Treaty provides a set of “tie-breaker rules” in the event each of the countries considers a person its domiciliary. The criteria are, in order:

- (a) Where did the person have a permanent home?
- (b) Where was the person’s center of vital interests or personal relations?
- (c) Where did the person have an habitual abode?
- (d) In which country was the person a citizen?⁶

Exception: Under the US-Netherlands Treaty, the first criterion is “where did the person have a permanent home for five years immediately preceding his death” and criterion (c)(habitual abode) is omitted. This Treaty uses closeness of personal relations as the sole criterion (b) but this may be seen as equivalent to center of vital interests, especially in light of the US-French Treaty, which mentions both and appears to treat them as the equivalent.⁷

⁵ FR4(3).

⁶ UK4(4), FR4(2), NETH4(3), GER4(2).

⁷ NETH4(3), see also FR4(2)(b).

III. Ten Scenarios Regarding the Allocation of Taxes and Tax Credits

1. European Citizen (i.e., a citizen of France, Germany, the Netherlands or the United Kingdom (“EC”)) who is a Domiciliary of one of the four countries (“European Domiciliary or ED”) or United States Citizen (“USC”) who is a European Country Domiciliary and who owns real property in the United States.

US collects its estate tax on the US real property of ECED or USCED. European Country (either the United Kingdom, France, the Netherlands or Germany) also imposes estate tax on the US real property but gives ECED’s or USCED’s heirs or estate a credit against the US tax.⁸

In addition: ECED’s or USCED’s “business property of a permanent establishment and assets pertaining to a fixed base used for professional services” located in the United States would be taxed in the same manner.⁹

The US will also apply a pro-rata share of the unified credit available to US citizens and domiciliaries to the tax on the US property of a French or German domiciliary who is not a U.S. citizen.¹⁰

If the U.S. tax on the worldwide estate of a UK domiciliary national, who was not a USC, computed as if the UK domiciliary national had become a USD immediately before death, is less than the US tax

⁸ UK6 and 9(2)(a), FR5 and 12(2)(a), NETH6 and 11(1); GER5 and 11(3)(a).

⁹ UK7, FR6, NETH7, GER6. The Netherlands Treaty clearly states that the fact that a decedent controlled a corporation that engaged in business in a country does not determine that the decedent had a permanent establishment in the country for estate or inheritance tax purposes. NETH7(7). The United Kingdom Treaty provides that the fact that a company residing in one country controls (or is controlled by) a company resident in the other country or doing business in the other country does not constitute either company a permanent establishment of the other. UK7(2)(g). The German Treaty has an analogous provision. GER6(2)(f). Finally, the French Treaty provides that the fact that an enterprise controlled a corporation that engaged in industrial or commercial activity in a country should not be taken into account in determining whether the enterprise had a permanent establishment in that country.

¹⁰ FR12(3), GER10(5).

*computed on a non-domiciliary basis, the U.S. tax can be computed as if the UK domiciliary national had died as a USD.*¹¹

Exception:

*The United States does not tax US real property or business establishment/fixed base property of Netherlands nationals if the property's value is less than \$30,000; in addition, the tax cannot exceed the lesser of 50% of the property's value in excess of \$30,000 or the amount of the tax determined in accordance with the Treaty after applying exemptions allowable under US law.*¹²

2. United States Domiciliary Citizen (“USCD”) or European Citizen who is United States Domiciliary (“ECUSD”) and who owns real property in European Country.

European Country collects its tax on the European real property of USCD. US imposes its tax on the European property as well but gives USCD's or ECUSD's estate a credit for the European Country tax on the European real property.¹³

*In addition: USCD's or ECUSD's “business property of a permanent establishment and assets pertaining to a fixed base used for professional services” located in the European Country would be taxed in the same manner.*¹⁴

*Netherlands does not tax Netherlands real property or business establishment/fixed base property of a US domiciliary if the property's value is less than \$30,000; in addition, the tax cannot exceed the lesser of 50% of value in excess of \$30,000 or the amount of the tax determined in accordance with the Treaty after applying exemptions available under Netherlands law.*¹⁵

¹¹ UK 8(5)

¹² NETH10(2). It appears that the “exemption” referred to here under U.S. law, is the \$60,000 exclusion available to non-resident alien estates and not the significantly higher applicable exclusion available to domestic estates.

¹³ UK6 and 9(1)(a), FR5 and 12(2)(b), NETH6 and 11(1), GER5 and 11(2)(a).

¹⁴ UK7, FR6, NETH7, GER6

¹⁵ NETH10(2).

3. ECED owns collection of paintings for personal use in the United States.

Save for the provisions of the French Treaty, US collects no tax on the US painting collection of ECED. European Country imposes its tax on the collection.¹⁶

The same rule would generally apply to other forms of tangible property in the United States not connected with a business establishment owned by ECED. In addition, the United States does not tax ships and aircraft engaged in international traffic belonging to a German domiciliary (“GD”) if the ships and aircraft are part of GD’s enterprise (presumably even if the enterprise constitutes a US business establishment).¹⁷

Exception: In the case of a French domiciliary (“FD”) FD’s tangible property (other than currency) located in US would be subject to US tax (except for property of certain persons (see II(3)(b)(ii) above) who held tangible property for personal use).¹⁸ Also, FD’s ships and aircraft operated in international traffic that are registered in the United States or that most frequently use the harbors and airports of the United States would be subject to US tax.¹⁹ Under these circumstances, France would give an effective credit for the U.S. tax on FD’s US tangible property.²⁰

¹⁶ UK5(1)(a) (excludes from US tax all property except for US real property and US business establishment property), FR8 (excludes from US tax all property except for US real property, US business establishment property and certain US tangible property (including certain ships and aircraft), NETH8 (excludes from Netherlands tax all property except for US real property and US business establishment property), GER9 (excludes from US tax all property except for US real property, US business establishment property, and interests in partnerships owning any of such US property).

¹⁷ GER7.

¹⁸ FR7(1)&(2).

¹⁹ FR7(3).

²⁰ FR12(2)(a).

4. USCD owns collection of paintings for personal use in European Country.

Save for the provision of the French Treaty, and an exception under the German Treaty noted below, European Country collects no tax on the European Country painting collection located in the European Country that is owned by USCD. US imposes its tax on the collection.²¹

The same rule would generally apply to other forms of tangible property in the European Country not connected with a business establishment owned by USCD. In addition, Germany does not tax ships and aircraft engaged in international traffic belonging to USCD if the ships and aircraft are part of USCD's enterprise (presumably even if the enterprise constitutes a German business establishment).²²

Exception: In the case of a USCD owning tangible property in France, such property (other than currency) would be subject to French tax (except for property of certain persons (see II(3)(b)(ii) above) who held tangible property for personal use).²³ Also, USCD's ships and aircraft operated in international traffic that are registered in France or that most frequently use the harbors and airports of France would be subject to French tax.²⁴ Under these circumstances, US would give a credit for the French tax.²⁵

Furthermore, Germany may tax an heir, donee or beneficiary domiciled in Germany on the tangible property of a USCD he or she receives from a USCD.²⁶

²¹ UK5(1)(a) (excludes from UK tax all property except for UK real property and UK business establishment/ fixed based property), FR8 (excludes from French tax all property except for French real property, French business establishment/ fixed based property and certain French tangible property (including certain ships and aircraft), NETH8 (excludes from Netherlands tax all property except for Netherlands real property and Netherlands business establishment/ fixed based property), GER9 (excludes from German tax all property except for German real property, German business establishment/ fixed based property, certain German-connected ships and aircraft, and interests in partnerships owning any of such German property).

²² GER7.

²³ FR7(1)&(2).

²⁴ FR7(3).

²⁵ FR12(2)(b).

²⁶ GER11(5)

5. ECUSD owns collection of paintings for personal use in European Country.

US imposes its tax on the collection owned by the ECUSD. European country is authorized to tax the collection of an EC on the basis of EC's nationality, although no European Country currently does so on this basis alone. If it did, European Country should give a credit against its tax for the US tax.²⁷

The same rule would generally apply to other forms of tangible property in a European Country not connected with a business establishment/fixed based owned by a ECUSD. In addition, Germany does not tax ships and aircraft engaged in international traffic belonging to a ECUSD if the ships and aircraft are part of ECUSD's enterprise (presumably even if the enterprise constitutes a German business establishment).²⁸

Exceptions:

In the case of a ECUSD owning tangible property in France, such property (other than currency) would be subject to French tax (except for property of certain persons (see II(3)(b)(ii) above) who held tangible property for personal use).²⁹ Also, ECUSD's ships and aircraft operated in international traffic that are registered in France or that most frequently use the harbors and airports of France would be subject to French tax.³⁰ Under these circumstances, US would give a credit for the French tax.³¹

Germany is effectively not permitted to tax on the basis of citizenship alone, although it may tax a heir, donee or beneficiary domiciled in Germany receiving tangible property from a US citizen or domiciliary.³²

In the case of a US domiciliary who is also a Netherlands citizen, Netherlands must give a full credit for US tax only if such

²⁷ UK5(1)(b) and 9(2), FR8 and 12(2)(a), NETH9 and 11(2).

²⁸ GER7.

²⁹ FR7(1)&(2).

³⁰ FR7(3).

³¹ FR12(2)(b).

³² GER 4(1), 11(1)(b).

Netherlands citizen-US domiciliary was a US domiciliary for 7 out of last 10 years.³³ Otherwise, each of the Netherlands and the US gives credit for that amount of tax paid to the other country that bears the same proportion to the less of its tax or the other country's tax attributable to the intangible property as that amount bears to total of both taxes.³⁴

6. USCED owns collection of paintings for personal use in the United States.

US and European country each imposes its respective tax on the US collection of the USCED. The US gives a credit for the EC tax against the US tax.³⁵

The same rule would generally apply to other forms of tangible property in the European country not connected with a business establishment/fixed based owned by USCED.

Exception:

In the case of a U.S. citizen who is a Netherlands domiciliary but is not a Netherlands citizen ("USCND"), US gives a full credit for Netherlands tax only if the USCND was Netherlands domiciliary for 7 out of last 10 years.³⁶ Otherwise, each of US and Netherlands gives credit for the amount of tax paid to the other country that bears same the proportion to the lesser of its tax or the other country's tax attributable to the intangible property as that amount bears to the total of both taxes.³⁷

³³ NETH11(2)(a).

³⁴ NETH11(2)(c). Example: Say the intangible property is worth \$1 million, the NETH tax is 40% and the US tax is 50%. The NETH tax would be \$400,000 and the US tax would be \$500,000 and the sum of both taxes would be \$900,000. NETH and US would each give a credit of 4/9 of its respective tax. The NETH tax would be \$222,222, the US tax would be \$277,777, and the total tax would be \$500,000. The objectives of the Treaty are fulfilled because the total of the two taxes does not exceed the higher of the two taxes.

³⁵ UK5(1)(b) and 9(1)(b), FR8 and 12(3), NETH9 and 11(2)(c) but see 11(2)(a) and (c), GER11(1), 11(2)(b)

³⁶ NETH11(2)(a).

³⁷ NETH11(2)(c). Example: Say the intangible property is worth \$1 million, the NETH tax is 40% and the US tax is 50%. The NETH tax would be \$400,000 and the US tax would be \$500,000 and the sum of both taxes would be \$900,000. NETH and US would each give a credit of 4/9 of its respective tax. The NETH tax would be \$222,222, the US tax would be \$277,777, and the total tax would be \$500,000. The objectives of the Treaty are fulfilled because the total of the two taxes does not exceed the higher of the two taxes.

7. ECED owns stock in US companies.

US collects no tax on the US stock of ECED. European Country imposes its tax on the stock.³⁸

*The same rule would generally apply to other forms of intangible property in the United States owned by ECED. However, interests owned by a German domiciliary in partnerships holding US real property and business establishment property may be taxed by the United States, and Germany would give a credit for the US tax.*³⁹

8. USCD owns stock in European companies.

European country collects no tax on the EC stock. US imposes its tax on the EC stock owned by USCD.⁴⁰

The same rule would generally apply to other forms of intangible property in the European country owned by USCD.

*However, interests owned by USCD in partnerships holding German real property and business establishment/ fixed based property may be taxed by Germany and the United States would give a credit against the German tax.*⁴¹

³⁸ UK5(1)(a) (excludes from US tax all property except for US real property and US business establishment/ fixed based property), FR8 (excludes from US tax all property except for US real property, US business establishment/ fixed based property and certain US tangible property (including certain ships and aircraft), NETH8 (excludes from US tax all property except for US real property and US business establishment/ fixed based property), GER9 (excludes from US tax all property except for US real property, US business establishment/ fixed based property, certain US-connected ships and aircraft, and interests in partnerships owning any of such US property).

³⁹ GER8 and 11(3)(a).

⁴⁰ UK5(1)(a) (excludes from UK tax all property except for UK real property and UK business establishment/ fixed based property), FR8 (excludes from French tax all property except for French real property, French business establishment/ fixed based property and certain French tangible property (including certain ships and aircraft), NETH8 (excludes from Netherlands tax all property except for Netherlands real property and Netherlands business establishment/ fixed based property), GER9 (excludes from German tax all property except for German real property, German business establishment/ fixed based property, certain German-connected ships and aircraft, and interests in partnerships owning any of such German property).

⁴¹ GER8 and 11(2)(a).

Furthermore, Germany may tax an heir, donee or beneficiary domiciled in Germany, who receives stock or other intangible property of a USCD.⁴²

9. ECUSD owns stock in European companies.

US imposes its tax on the European Country stock owned by ECUSD. European Country is authorized to tax the stock, although no European Country currently does so on this basis alone. If it did, it should give a credit for the US tax.⁴³

The same rule would generally apply to other forms of intangible property in the European Country owned by ECUSD.

Exceptions:

While France is not precluded from taxing on the basis of French nationality, there is no effective credit under the US-France Treaty if it did.⁴⁴

Germany is effectively not permitted to tax on the basis of citizenship alone, although it may tax a German heir, donee or beneficiary receiving stock or other intangible property from a US citizen or domiciliary.⁴⁵ Also, interests owned by ECUSD in partnerships holding German real property and business establishment property may be taxed by Germany and the United States would give a credit for the German tax.⁴⁶

In the case of a US domiciliary who is a Netherlands citizen, Netherlands must give a full credit for the US tax only if such Netherlands citizen-US domiciliary was a US domiciliary for 7 out of last 10 years.⁴⁷ Otherwise, each of the Netherlands and the US gives credit against its tax for that amount that bears the same proportion to the less of its tax or the other

⁴² GER11(5)

⁴³ UK5(1)(b), 6 and FR5, 8 and 12(2)(a), NETH6, 9, 11(1)&(2), GER5 and 11(2)(a).

⁴⁴ FR12(2)(a).

⁴⁵ GER 4(1), 11(1)

⁴⁶ GER8 and 11(2)(a).

⁴⁷ NETH11(2)(a).

*country's tax attributable to the intangible property as that amount bears to the total of both taxes.*⁴⁸

10. USCED owns stock in US companies.

US and European Country each imposes its respective tax on the US stock. The US gives a credit for the European Country tax.⁴⁹

The same rule would generally apply to other forms of intangible property in the United States owned by USCED.

Exceptions:

*Interests owned by USCED in partnerships holding US real property and business establishment/fixed based property may be taxed by the United States and Germany would give a credit for the US tax.*⁵⁰

*In the case of a US citizen who is a Netherlands domiciliary, the US gives a full credit for the Netherlands tax only if the U.S. citizen-Netherlands domiciliary was a Netherlands domiciliary for 7 out of the last 10 years.*⁵¹ *Otherwise, each of the US and Netherlands gives a credit against its tax for that amount that bears the same proportion to the lesser of its tax or the other country's tax attributable to the intangible property as that amount bears to the total of both taxes.*⁵²

⁴⁸ NETH11(2)(c). Example: Say the intangible property is worth \$1 million, the NETH tax is 40% and the US tax is 50%. The NETH tax would be \$400,000 and the US tax would be \$500,000 and the sum of both taxes would be \$900,000. NETH and US would each give a credit of 4/9 of its respective tax. The NETH tax would be \$222,222, the US tax would be \$277,777, and the total tax would be \$500,000. The objectives of the Treaty are fulfilled because the total of the two taxes does not exceed the higher of the two taxes.

⁴⁹ UK5(1)(b) and 9(1)(b), FR8 and 12(3), NETH9 and 11(2)(c) but see 11(2)(a) and (c), GER11(1), 11(2)(b)

⁵⁰ GER8 and 11(3)(a).

⁵¹ NETH11(2)(a).

⁵² NETH11(2)(c). Example: Say the intangible property is worth \$1 million, the NETH tax is 40% and the US tax is 50%. The NETH tax would be \$400,000 and the US tax would be \$500,000 and the sum of both taxes would be \$900,000. NETH and US would each give a credit of 4/9 of its respective tax. The NETH tax would be \$222,222, the US tax would be \$277,777, and the total tax would be \$500,000. The objectives of the Treaty are fulfilled because the total of the two taxes does not exceed the higher of the two taxes.

IV. Other Topics

A. Charitable Deductions

1. There are no special rules in the US-UK or US-Netherlands Treaties.
2. US-Germany: Reciprocal charitable deduction for donor country persons for transfers to charitable organizations and public bodies in the other country if the transfer would be exempt from tax in the donee country and transfer would be exempt in the donor's country if the gift were made to a similar charity or public body in the donor's country.⁵³
3. US-France: Same essential rule as with Germany but the charitable organization must receive a substantial part of its support from contributions from the public or governmental funds.⁵⁴

B. Marital Deductions

1. US-UK: In the case of property passing to the spouse of a decedent who was a US citizen or domiciliary, UK will allow a 50% marital deduction even if the spouse is not domiciled in the UK.⁵⁵
2. US-France: Property (other than community property) acquired during marriage by US citizen or domiciliary shall be treated for French tax purposes as community property (in the absence of a contrary election).⁵⁶ There is also available a US marital deduction limited to the US applicable exclusion for property passing from a US or French domiciliary or US citizen to a US or French surviving spouse, if an election not to use a QDOT to secure any additional marital deduction is made.
3. US-Netherlands: Real property and business establishment/fixed based property (other than community property) passing to surviving spouse from a US citizen or domiciliary shall be included in the estate for purposes of the

⁵³ See GER10(2)

⁵⁴ FR10(2).

⁵⁵ UK8(3).

⁵⁶ FR11.

Netherlands death duty only to the extent its value exceeds 50% of all property taxable by the Netherlands. Value of property is determined after taking into account allowable deductions but before taking into account the treaty exclusion of property with a value under \$30,000.⁵⁷

4. US-Germany: Real property, business establishment/fixed based property (other than community property), and certain ships and aircraft passing to a surviving spouse from a citizen or domiciliary of either country that may be taxed by a country because the property is located there may only be taxed to the extent its value exceeds 50% of all property taxable by that country.⁵⁸ There is also available a US marital deduction limited to the US applicable exclusion for property passing from a US or German domiciliary or US citizen to a US or German surviving spouse, if an election not to use QDOT to secure any additional marital deduction is made.⁵⁹

C. U.S. Applicable Exclusion (“Unified Credit”)

1. US-France: US will apply a pro-rata share of the applicable exclusion available to US citizens and domiciliaries to the tax on the U.S. property of a French domiciliary who is not a US citizen.⁶⁰

2. US-Germany: US will apply a pro-rata share of the applicable exclusion available to US citizen and domiciliaries to the tax on the US property of a German domiciliary who is not a US citizen.⁶¹

3. US-United Kingdom: In the case of US tax permitted to be imposed by the US-UK Treaty on the US property of a UK citizen who was neither a US citizen nor a US domiciliary, that UK citizen’s estate may make a claim to limit the US tax to that amount of US tax that would have been imposed if that UK citizen had become domiciled in the US immediately before death on the property that would have been taxable in that event (basically the UK citizen’s worldwide estate).

⁵⁷ NETH10(1).

⁵⁸ GER10(4).

⁵⁹ GER10(6).

⁶⁰ FR 12(3).

⁶¹ GER 10(5).

Thus, in the relevant case, such a UK citizen may claim the benefit of the unified credit (i.e., the applicable exclusion) available to a US citizen or domiciliary (2018: \$11,180,000 applicable exclusion instead of the \$60,000 exclusion allowed to non-US decedent estates) in a calculation that assumes the US has the right to tax that UK citizen's worldwide estate. In situations where the US property on which the US is allowed to impose US tax under the Treaty represents a significant portion of the worldwide estate, this could result in a significant reduction or even elimination of the US tax.⁶²

D. US State Death Taxes

According to the US-Germany Treaty, certain credits allowed by Germany may also include "taxes levied by political subdivisions of the United States."⁶³

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⁶² UK 8(5).

⁶³ GER11(4).