

# Welcome To The USA: The Rising Popularity Of US-Situs Trusts - Part One

**TODD BEUTLER AND TODD MAYO**

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*Here, Todd Beutler of the global law firm DLA Piper, and Todd Mayo of Perspecta Trust, outline why international families are increasingly turning to the US for the creation of trusts.*

*Beutler is co-head of DLA Piper's global private client group, based in Hong Kong. Mayo is a principal and general counsel at Perspecta Trust, based in Hampton, NH.*

*As ever, Family Wealth Report does not necessarily agree with all of the comments herein, but is delighted to publish them and welcomes reader responses.*

Across the globe, there are a number of attractive jurisdictions for trusts. Among them are a handful of US jurisdictions. More and more, wealthy families are including US-situs trusts in their wealth planning structures. Several factors—including investment opportunities, wealth preservation, tax planning, and good laws—are motivating non-US families to use US-situs trusts.

## Investing in the US

Many families are looking to invest in the US. Right now, much of the investment activity involves US real estate. The *Wall Street Journal*, *International Business Times*, CNN, and other media outlets have recently spotlighted investment by Chinese families, who currently are the largest group of foreign real estate buyers in the US. As the *Wall Street Journal* reported, "signs are emerging that Chinese property investments abroad will maintain their torrid pace despite the market turmoil, as wealthy individuals and well-heeled companies seek to shelter their money in more stable havens abroad." While recent media reports have focused on Chinese investment in the US, Chinese families are not alone. Wealthy families from elsewhere in Asia, as well as from Europe, the Middle East, and South America, are investing in the US.

For families investing in the US, a US-situs trust often is the optimal top-tier vehicle for holding those investments. If a family already has a non-US situs trust or foundation, a US-situs trust can readily complement the family's existing arrangement for managing its wealth. If properly designed, a US-situs trust is a tax-efficient way through which to hold US real estate or other US assets, and it can minimize the family's exposure to US income, gift, and estate taxes.

## Preservation of family wealth

For some families, the US is a place in which to safeguard their wealth. In their home countries, they face political, social, and economic uncertainties. Those uncertainties may even include the risk of expropriation. For those families, investment opportunities may be secondary to simply preserving the wealth that they already have accumulated. They look to the US as a safe haven for their wealth, because it offers political stability, a well-established rule of law, and access to the markets. They create US-situs trusts or move existing trusts to the US, because they want to have peace of mind that their wealth is protected.

## Pre-immigration planning

Individuals and families considering immigrating into the US often use US-situs trusts as a part of their pre-immigration tax planning. For someone considering a temporary or permanent move to the US, a US-situs trust potentially can play a significant role sheltering income from US income taxes and sheltering assets from US estate taxes.

Becoming a US citizen or US resident carries a tax burden. For income tax purposes, the US taxes a nonresident, non-citizen only on US-source income. In contrast, the US taxes a US citizen or a US resident on his or her worldwide income. For estate tax purposes, the US taxes a nonresident, non-citizen only on US-situs property. In contrast, the US taxes a US citizen or a US resident on worldwide assets. Pre-immigration tax planning can minimize that tax burden.

While there are many facets to pre-immigration tax planning, trusts often play an integral part of a comprehensive plan. A drop-off trust, for example, is a common strategy for minimizing exposure to US estate taxes. Under the terms of the trust, the individual must not retain any impermissible rights or control, such as the power to direct distributions. The individual, however, generally can retain the power to manage the trust property.

If the trust is created in a US jurisdiction that, like New Hampshire, recognizes self-settled spendthrift trusts, then the individual can be a discretionary beneficiary. Care in the design and implementation, however, is required if the individual is a beneficiary. Given the trust's tax deferral benefits, it is advantageous to create the trust in a US jurisdiction that, like New Hampshire, allows perpetual private trusts.

## Other tax considerations

US income tax law often motivates multi-national families to move existing trusts to the US. If a non-US trust has a US beneficiary, there can be unwelcome tax consequences. The US beneficiary potentially faces significant, enhanced taxes upon receipt of a distribution from the trust. In addition, the US beneficiary may be taxed upon receipt of a loan from the trust or upon the use of trust property, such as trust-owned real estate or artwork. Those unfavorable tax consequences most frequently arise after the settlor's death, and they disappear if the trust becomes a US trust for US tax purposes. Consequently, families and trustees generally will seek to "domesticate" or "on-shore" a non-US situs trust soon after the settlor's death.

While domestication often is advisable, it is not always optimal. When a settlor of a non-US trust dies, a family should not robotically domesticate the trust, even though that is the standard advice of many advisors. A thoughtful, holistic evaluation of the family's wealth planning, circumstances, and long-term plans may suggest a better approach.

## Tax reporting

With the rise of information sharing among countries concerning their citizens' and residents' assets and income—precipitated by the US's FATCA requirements—the US ironically has become a more attractive jurisdiction for trusts. Compliance with reporting obligations can be simpler when a US financial institution is serving as a trustee of a trust. Moreover, contrary to popular belief, the US recognizes a US-situs trust that, for US tax purposes, is a non-US trust. The US treats that "non-US trust" in the same manner as, for example, it would a Jersey-situs trust or a Cayman-situs trust.

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