

# Estate Planning for Foreign Nationals Using Life Insurance

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INSURANCE PRODUCTS:		
NOT INSURED BY FDIC OR ANY FEDERAL GOVERNMENT AGENCY	MAY LOSE VALUE	NOT A DEPOSIT OF OR GUARANTEED BY ANY BANK OR ANY BANK AFFILIATE



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Bring Your Challenges™

# Why Do You Need to Plan?

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- Foreign nationals may be subject to U.S. income, estate, and gift tax
- Foreign nationals have similar life insurance needs as U.S. citizens: wealth transfer, estate planning, income protection and business continuation

# Why This Market?

- Large market with large case potential
- Ties in with Institutional Marketing efforts
  - good lead source
- Desire for:
  - US denominated mortality based products
  - Capacity (due to minimal coverage available domestically)
  - Stability

# Foreign Nationals in the U.S.

## Large market with large case potential

- The 2010 U.S. Census found 309.4 million U.S. residents.
- 39.9 million are foreign born.
- 22.5 million are foreign-born & non-citizens.
- Non-citizens represent 7.3% of total U.S. population.
- Non-citizen residents tend to have dependents & protection needs.

\*Source: The Foreign-Born Population in the United States: 2010. American Community Survey Reports. Found at: [www.census.gov/prod/2012pubs/acs-19.pdf](http://www.census.gov/prod/2012pubs/acs-19.pdf). Accessed on: January 9, 2013.

# Why Consider Prudential?

- Retention and Reinsurance Capacity
- Market Experience
- Ability to manage jumbo cases
- Reliability and Financial Strength
- Brand
- Competitive Products — single and limited pay scenarios

# Terminology

- “Alien” describes a person who is not a U.S. citizen
- “Resident alien” and “non-resident alien” distinctions
- Different U.S. income, estate and gift-tax tests

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# RESIDENT ALIENS

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# Resident Alien for U.S. Estate & Gift Tax Purposes

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- Non-U.S. citizen
- “Domiciled” in the U.S.



# Domicile vs. Residence

- **Domicile** is a person's fixed and permanent home
  - Center of a person's domestic and legal relations with no present intention of leaving
  - Can have only **one** domicile
- **Residence** signifies where someone is living at a given point in time
  - Can have **more than one** residence

## Factors IRS Considers to Determine Domicile

- Duration of stay in U.S. relative to other countries
- Amount of travel between U.S. and other countries
- Size and cost of homes and whether they are owned or rented
- Location of expensive and personal possessions
- Location of family and close friends
- Location of business interests, religious and club memberships
- Motivation for being in U.S. (health, pleasure, business, etc.)
- Immigration status
- Declaration of residence in legal documents (wills, trusts, etc.)

# U.S. Citizen or Resident Alien

<b>U.S. Estate Tax:</b>	<b>Worldwide property owned by decedent subject to taxation</b>
<b>U.S. Gift Tax:</b>	<b>Worldwide gifts subject to taxation</b>
<b>U.S. Generation Skipping Tax:</b>	<b>Generation-skipping gifts and bequests subject to taxation</b>
<b>U.S. Annual Gift Tax Exclusion:</b>	<b>\$14,000* \$145,000 for gifts to non-U.S. citizen spouse*</b>

\*2014 amounts, indexed annually for inflation the following years

# U.S. Citizen or Resident Alien

<b>Marital Deduction</b>	<b>Unlimited transfers to U.S. citizen spouse If Qualified Domestic Trust established, then unlimited transfers at death to non-U.S. citizen spouse</b>
<b>Exclusion Amount for Transfers during Life and/or Death</b>	<b>\$5,340,000*</b>
<b>Gift Splitting</b>	<b>As long as both spouses are U.S. citizens or resident aliens</b>

\*2014 amounts, indexed annually for inflation the following years

# Qualified Domestic Trust (QDOT)

## Authority:

- IRC §2056A(a) and regulations there under
- Highlights:
  - All income must be paid to the surviving spouse for life
  - One trustee must be a U.S. citizen or domestic corporation
  - U.S. trustee must be able to withhold QDOT tax on any distributions of trust principal
  - Executor of estate must make QDOT election on timely, filed federal estate tax return
  - QDOT must satisfy other marital deduction rules

# Taxation of QDOTs

## QDOT tax imposed on the following:

- Lifetime distributions of principal
  - Taxed at the federal estate tax amount that would have been imposed on estate of decedent spouse had decedent's taxable estate been increased by the amount of the distribution
- Death of surviving spouse
  - Assets remaining in QDOT valued as of date of death of surviving spouse and taxed as if it were included in estate of decedent spouse
- Trust ceases to qualify as QDOT
  - Fair market value of QDOT assets on the date of disqualification taxed as if it were included in estate of decedent spouse

## QDOT Distributions Exempt from QDOT Tax

- Distributions from income
- Distributions on account of hardship
  - No real definition of hardship
    - Generally, if distribution is in response to immediate and substantial financial need relating to spouse or someone spouse has a legal obligation to support for health, education, or maintenance
    - Not a hardship exemption if amount distributed could be obtained from other sources reasonably available to spouse

# NON-RESIDENT ALIENS (NRAs)



# NRA For Estate & Gift-Tax Purposes

For U.S. estate & gift-tax purposes

- Non-U.S. citizen “domiciled” outside of the United States

# Non-Resident Alien

<b>U.S. Estate Tax:</b>	U.S. situs property owned by decedent subject to taxation Non U.S. situs property and certain property specifically not considered U.S. situs property not subject to taxation
<b>U.S. Gift Tax:</b>	Gifts of tangible U.S. situs property subject to taxation Gifts of intangible U.S. situs property and gifts of non-U.S. situs property not subject to taxation
<b>U.S. Generation Skipping Tax:</b>	Generation skipping gifts and bequests subject to U.S. estate or gift tax subject to taxation
<b>U.S. Annual Gift Tax Exclusion:</b>	\$14,000* \$145,000 for gifts to non-U.S. citizen spouse*

\*2014 amounts, indexed annually for inflation the following years

# Non-Resident Alien

<b>Marital Deduction</b>	<i>Unlimited transfers to U.S. citizen spouse</i> <i>If QDOT established, then unlimited transfers at death to non-U.S. citizen spouse</i>
<b>Applicable Exclusion Amount for Transfers at Death</b>	<i>\$60,000</i>
<b>Gift Splitting</b>	<i>Not possible</i>

# Life Insurance on NRA

- For years in which there is a Federal estate tax, IRC §2105(a) specifically excludes life insurance proceeds on the life of the NRA from the NRA's U.S. gross estate
- **NRA can own a life insurance policy on his/her own life, and provide a death benefit to his/her family both U.S. federal income and estate-tax free!**

*But what about access to policy cash value?...*

# Life Insurance & NRA

## Tax issues:

- Cash value (CV)
  - Under U.S. Income Tax Law, CV accumulates tax-deferred
  - No U.S. income tax on accumulated value
- Loans and withdrawals\*
  - Under U.S. income tax law, NRA has income-tax free access to policy's CV through loans and withdrawals
  - NRA can access CV without U.S. federal income tax

\*Depending upon the performance of a VUL policy's investment choices, the account value may be worth more or less than the original amount invested in the policy.

# Life Insurance & NRA

- **Death benefits**
  - Generally under U.S. income tax law, death benefit proceeds are received by beneficiaries income-tax free\*
  - NRA's beneficiary receives proceeds U.S. income-tax free
  - Not part of NRA's U.S. taxable estate [IRC 2105(a)]
- **Surrender, lapse or maturity**
  - If gain in contract on surrender, lapse or when policy matures, then U.S. income taxable event
  - NRA is subject to flat 30% federal income tax\*\*

\*Keep in mind: Proceeds are received income tax-free as long as the policy meets definition of life insurance and wasn't transferred for valuable consideration. If a policy fails to meet definition of life insurance, inside buildup plus cost of insurance is subject to tax each year while the insured is alive but the death benefit is still income tax free.

\*\*If the policy connected to U.S. trade or business, ordinary income tax rates apply

## Tax Treatment of Life insurance by Countries other than U.S.

- This presentation is primarily about the U.S. tax treatment of life insurance owned by a foreign national
- The income, gift and estate tax treatment of a U.S. issued life insurance policy owned by a foreign national will depend on each country's own laws
- Clients should consult with tax counsel knowledgeable about the tax rules in their country of residence and/or citizenship. The countries where foreign nationals reside may also have their own rules regarding the tax treatment of life insurance proceeds and clients should consult with their tax and legal advisors to understand the tax treatment of the policy by other countries. In addition, some non-U.S. countries may impose fines and/or penalties (civil and criminal) against their residents or citizens who purchase a U.S. issued life insurance policy and clients should consult with their advisors to understand whether any such fines and/or penalties are applicable.

# U.S. Tax Treaties With Foreign Countries

- U.S. has income, estate and gift tax treaties with many countries to avoid double taxation, expand deductions and exchange information
- U.S. has estate tax treaties with:
  - Australia, Austria, Denmark, Finland, France, Germany, Greece, Ireland, Italy, Japan, Netherlands, Norway, South Africa, Switzerland and United Kingdom
- U.S. has gift tax treaties with:
  - Australia, Austria, Denmark, France, Germany, Japan and United Kingdom



# Prudential's Underwriting for Non-US Residents

- For underwriting purposes, A Non-US Resident is individual who:
  - Spends > six months a year outside of US
  - Visits US for business or pleasure but maintains permanent residence outside of US
  - Is expected to reside in US on a temporary basis
  - Resides in US on a part time basis only

## Basic Underwriting Requirements for Non-U.S. Residents

- All activities including solicitation, completion of the application, call interview, medical examination and contract delivery must take place in the US
- Consideration extended to business owners, professionals in medical, engineering, scientific, technological or similar fields and immediate families
- Ongoing health maintenance record with most recent visit within 3 years
- Medical Exam, Blood, Urine, ECG based on normal age and amount rules
- Attending Physician Statements, including foreign ones
- Data Verification Report
- Third-Party Financial Documentation for face amounts of \$1 million and above
- Copy of Government issued photo ID (such as Passport)

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# Basic Underwriting Requirements for Non-U.S. Residents (cont.)

- Version of Form W-8 for those without a Social Security Number
- Individuals active in foreign military, police, government or judicial services within resident country will not be considered for coverage.
- Minimum face amount is \$250,000
- Automatic limits of \$20 million on individuals residing in acceptable countries may be considered depending on various facts and circumstances
- Max issue age is 75 for reinsured cases and 70 for fully retained cases
- Premiums paid annually and in US currency

# Non-US Residents Highlighter

- Marketing Piece( 0156067) and PruXpress must be consulted to determine what resident countries are acceptable and unacceptable for coverage. These guidelines change based on analysis of government, travel services, industry data and current conditions.
- Countries are classified as follows:
  - A, Acceptable for Residence-Preferred Best available
  - B, Acceptable for Residence-Non-Smoker Plus available
  - C, Unacceptable for Residence
  - Some countries' residents are not permitted to purchase insurance from an unauthorized insurer, under many circumstances. These countries are identified on PruXpress via Blue Text. .

# Important Information

This material provides general information in regard to the subject matter covered. It should be used with the understanding that we are not rendering legal, accounting or tax advice. Such services should be provided by the client's own advisors. Accordingly, any information in this document cannot be used by any taxpayer for purposes of avoiding penalties under the Internal Revenue Code.

Rates and availability will vary based on the satisfaction of our underwriting criteria. Underwriting rules are subject to change at our discretion

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