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Practical Guide on US Estate & Gift Tax

June 2026

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US Estate & Gift Tax

A Guide for Indian Families with US Ties

The United States imposes estate and gift tax not just on its citizens, but also on non-residents who hold US-situs assets. For Indian families with US investments, US-citizen children, or returning green card holders, understanding this framework is essential. This guide works through who is exposed, what assets are at risk, and what families can do to plan for it.

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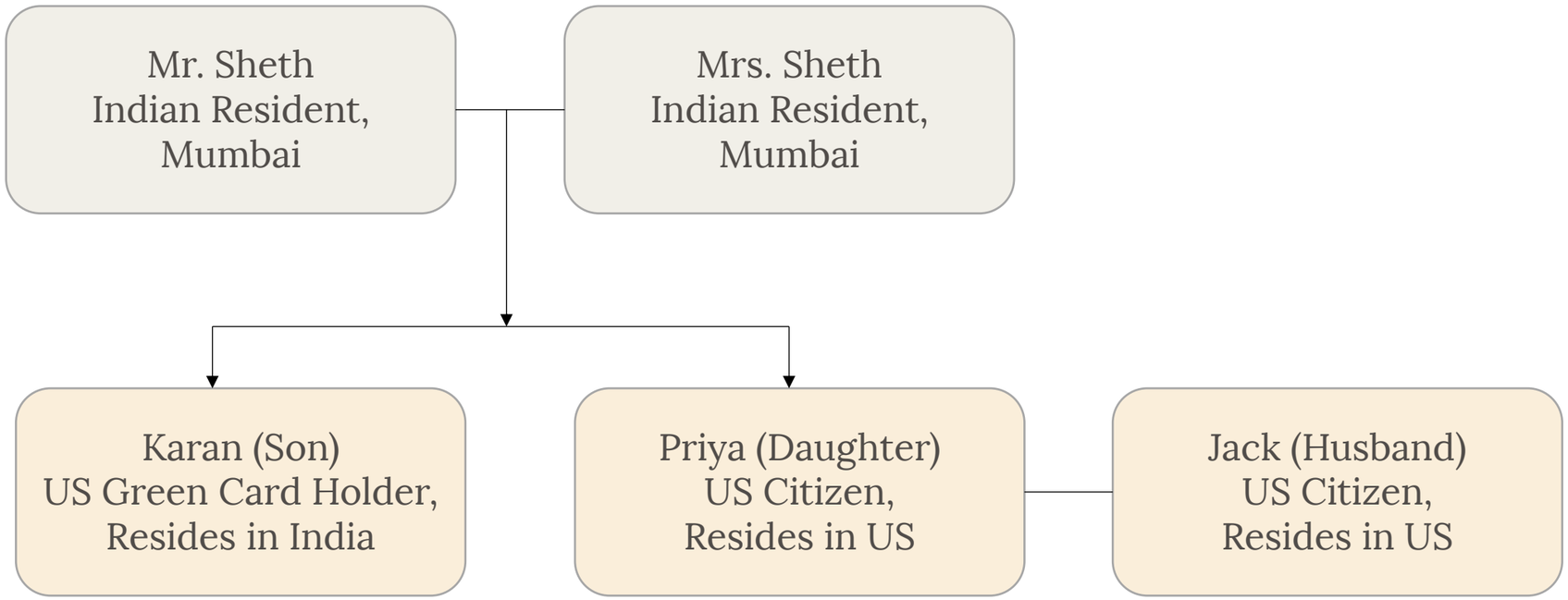
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Setting the Context

Meet the Sheth family.

Mr. Sheth, an Indian resident and Indian citizen based in Mumbai, has built a successful textile business over the years. Like many affluent Indian investors, he also invested part of his wealth in US-listed stocks such as Apple, Microsoft, Tesla, etc. through an offshore brokerage account. A few years ago, he purchased a small apartment in New York for family visits and investment purposes.

His son Karan studied in the US, obtained a green card, and eventually returned to India to join the family business. His daughter Priya later moved to the US, became a US citizen, and now lives there with her husband (who is also a US citizen). At first glance, this may look like a fairly ordinary global Indian family. But from a US estate and gift tax perspective, each family member falls into a completely different category and that changes everything.



What this Means

US estate tax is a tax on the wealth a person leaves behind at death, paid by their estate rather than by the family who inherits. It can reach either everything they owned worldwide, or only what they owned in the US. Which one applies depends on how closely the person was tied to the US, and that is where Mr. Sheth, Priya and Karan differ.

If Mr. Sheth were to pass away holding US assets directly, the US could impose estate tax at rates of up to 40%, despite him never being an American citizen or resident.

Priya, as a US citizen, is exposed to US estate tax on her worldwide assets. Karan sits somewhere in between, because green card holders who return to India can still remain connected to the US tax system depending on their facts and circumstances.

This piece is written for Indian families with US ties. It works through three questions:

- When does US estate or gift tax apply and to whom?
- What assets does it reach, and what assets does it not?
- What can families do to plan for it?

The Big Picture: US Tax Framework

> *The US tax framework broadly works through two separate systems. While both are relevant for Indian families with US ties, they operate on different connecting factors and apply to different types of transactions.*

Income Tax System

Taxes income as and when it is earned.

What It Covers

Salary, business profits, capital gains, interest, and dividends.

Connecting Factor

Citizenship or residency (physical presence or green card status).

Who Is liable to pay?

US citizens, green card holders, and individuals meeting the substantial presence test are taxed on worldwide income.

Transfer Tax System

Taxes the passing of wealth from one person to another – during lifetime or upon death.

Estate Tax

Tax on transfer of assets upon death. Maximum federal rate: 40% [1]

Gift Tax

Tax on transfer of assets during lifetime. Maximum federal rate: 40%

Connecting Factor

Citizenship or domicile - NOT the same as income tax residency.

Who Is liable to pay?

US citizens and domiciliary on worldwide assets. NRNCs on US-situs assets only.

The two systems are independent of each other. A person may be a US income tax resident without being a US domiciliary for transfer tax purposes - and vice versa.

What Matters for Estate & Gift Tax

> *The scope of US estate and gift tax is determined by two connecting factors: citizenship and domicile. A US citizen or US domiciliary is subject to US estate and gift tax on worldwide assets, irrespective of where those assets are located or where the individual resides.*

Citizenship: A Legal Status

Citizenship is established by law and documentary evidence and does not depend on personal circumstances or intentions.

Domicile: A Factual Determination

Domicile is the place an individual treats as a permanent home. US domicile arises when a person is present in the US with the intention to remain indefinitely[2]. Once US domicile is acquired, it continues until a new domicile is established elsewhere.

No single factor is decisive and there is no day-count test. The position is judged on all the facts, including:

- personal, family,
- business, and economic ties.
- No single factor is conclusive, and there is no prescribed day-count test.

Scenario 1 : Mr. Sheth and the $60,000 Trap

> *Mr. Sheth is a typical example of an Indian investor with unintended US estate tax exposure. He is neither a US citizen nor a US domiciliary. Accordingly, he falls under the category of a non-resident non-citizen (NRNC) for US estate tax purposes. For NRNCs, the US estate tax applies on specified US-situs assets and not on worldwide assets. The exemption is just $60,000 – not $15 million. Beyond this threshold, estate tax rates can go up to 40%.*

What Are US-Situs Assets?

For an NRNC, commonly encountered US-situs assets include:

- shares of US companies;
- US-listed ETFs and mutual funds;
- and US real estate.

The situs of a share follows the place of incorporation of the issuer, not the location of the brokerage account or share certificate. [3] Routing the same Apple shares through a Singapore or Dubai brokerage does not change the answer.

What Is Generally Not US-Situs?

Certain assets are generally outside the US estate tax net for NRNCs, such as:

- shares of non-US companies;
- bank deposits with US banks (so long as not effectively connected with a US trade or business); [4]
- certain debt instruments; and
- life insurance proceeds on the life of an NRNC.

This distinction becomes important from estate planning perspective.

Both Mr. Sheth's US-listed stock portfolio and his New York apartment fall within the US estate-tax net on his demise. Some states in the US also levy state estate tax with a much lower exemption threshold.

The Gift Tax Asymmetry

> *One of the more interesting aspects of the US transfer tax system is that estate tax and gift tax do not always apply in the same manner. For an NRNC, US gift tax generally does not apply to gifts of intangible assets (e.g., shares of a US company), even if those assets may otherwise be exposed to US estate tax upon death.* [5]

Lifetime Gifting of US Shares

Mr. Sheth may gift US-listed shares to his children during his lifetime without triggering US gift tax. However, if the same shares are held until death, they may become subject to US estate tax. This creates a meaningful planning opportunity.

US Real Estate: Both Taxes Apply

US real estate sits on the other side of this line. A gift of US real property, or of tangible personal property located in the US, is within the scope of US gift tax, and that property remains exposed to US estate tax if it is held until death.

Annual Exclusion

It is only on the US-situs real and tangible gifts that the annual exclusion has any role to play. For 2026 the exclusion is $19,000 per donee per year, and it reduces the value of such a gift that is counted for US gift tax. It does not apply to a gift of US-listed shares, because that gift falls outside the US gift tax net to begin with.[6]

Practically, this asymmetry between estate tax and gift tax on intangibles is one of the most important planning levers available to Indian families with US-listed investments.

Scenario 2 : Priya, the US Citizen

> *Priya sits at the opposite end of the spectrum from Mr. Sheth. As a US citizen, Priya is subject to US estate and gift tax on her worldwide assets, including Indian shares, real estate, and family business interests.*

Larger Exemption

US citizens have a much larger exemption: $15 million per person for 2026, with portability of any unused portion to a surviving citizen spouse. [7]

Step-Up in Basis

'Basis' means the tax cost of an asset. Inherited assets generally receive a fresh tax basis equal to their FMV at the time of death. This can significantly reduce capital gains tax when the assets are eventually sold. For example, if Priya inherits Indian assets from Mr. Sheth having an original cost of $100, and the fair market value on Mr. Sheth's demise is $500, then Priya's basis would become $500. If she later sale it at $500, there is no capital gain tax; she is taxed only on any increase above $500.

Reporting Trap: Form 3520

If Priya receives more than $100,000 in a calendar year by way of gift or bequest from any non-US individual (Mr. Sheth included), she must file Form 3520 with her US tax return. The penalty for missing it is 5% of the unreported amount for each month the gift/bequest goes unreported, with the total capped at 25% of that amount.

- The same benefit of step-up in basis is generally not available in case of lifetime gifts. In a gift, the donee typically receives the carryover basis of the donor, which is why the timing of transfer may become important.

Scenario 3: Karan, the Returning Green Card Holder

> *Karan moved back to India to join the family business after spending several years in the US. While he now lives in India full-time, he still holds a US green card. For US estate and gift tax purposes, the key concept is domicile - not merely immigration status. The question is whether Karan still treats the US as his permanent home.*

If Genuinely Shifted Back to India

If Karan has genuinely shifted his life back to India - family in India, business in India, no intention to settle back in the US - he may no longer be treated as US domiciled.

In that case, only specified US-situs assets remain exposed to US estate tax like in the case of NRNC.

If US Connection Remains Strong

If his facts continue to indicate a strong US connection, the US may still seek to treat him as US domiciled, potentially exposing his worldwide assets to the US transfer tax regime. On his demise, worldwide assets are exposed to US estate tax.

This is why returning green card holders should review their position carefully. The surrounding facts and conduct become just as important as the paperwork itself.

Scenario 3 (cont.): The Exit Tax Problem

> *If Karan eventually surrenders his green card, and he is considered a 'Covered Expatriate' on the exit date, then IRS will assume that Karan sold all his worldwide assets at fair market value the day before. He pays capital gain on deemed gain but the first $910,000 of gain (2026 figure, indexed annually) is excluded. The capital assets are taxed at up to 20% + 3.8% NIIT; retirement accounts (IRAs/HSAs) at ordinary rates up to 37%.*

What is a Covered Expatriate

Typically, a former US citizen or long-term green-card holder (green card holder in at least 8 of the last 15 years) who gave up that status after 2008 and, on the expatriation date, met any one of three tests.

The Three Tests

- Net worth of $2 million or more;

OR

- average annual US income-tax liability for the 5 preceding years above $211,000 (2026 figure);

OR

- failed to certify 5 years of US tax compliance on Form 8854.[8]

After Exit Tax Effects

The exit tax is a one-time tax triggered upon expatriation.

Separately, if Karan is a covered expatriate, any subsequent **gift or bequest** made by him to a US person - including a future gift to Priya (his US sister) - attracts a **40%** transfer tax payable by the **US recipient**.[9]

The principal considerations are the immediate exit tax and the potential 40% transfer tax on future wealth transfers to US persons.

What Can Families Do to Plan for It

> *The good news is that most US estate and gift tax exposure can usually be identified and planned for in advance. The right approach depends on several factors, including the type of assets involved, whether family members are US citizens, green card holders or Indian residents, and where the family intends to eventually settle.* Further, domicile and residency positions should also be reviewed carefully before moving into or out of the US.

Holding US Investments Through a Non-US Company

Some families hold US investments through a non-US company (such as a Mauritius, Singapore or BVI company) instead of holding US assets directly. This may help reduce US estate tax exposure, though other tax implications may also need to be evaluated.

Trust Structures for the Next Generation

For families with US-citizen children, appropriately structured irrevocable trusts settled by Indian parents may help keep assets outside the children's future taxable estates. However, foreign trust rules under the US tax system are highly technical and require careful structuring.

Life Insurance for Liquidity

Life insurance proceeds on the life of an NRNC are generally not treated as US-situs assets. Accordingly, insurance is often used to provide liquidity for any residual estate tax liability.

Lifetime Gifting of US Shares

US gift tax generally does not apply to gifts of intangible assets by an NRNC. Accordingly, an Indian parent may gift US-listed shares during lifetime instead of holding them until death.

The Non-US Citizen Spouse Issue

> *Where both spouses are US citizens, transfer of assets between them is generally not subject to US estate or gift tax. Where the surviving spouse is not a US citizen, the unlimited marital deduction does not apply. Lifetime gifts by US citizen spouse to non-US citizen spouse get an annual exclusion of $194,000 (2026). [10]*

QDOT: Qualified Domestic Trust

In cases where the surviving spouse is not a US citizen, a Qualified Domestic Trust (QDOT) may help defer US estate tax. A QDOT may be established either during the US citizen spouse's lifetime or under the US citizen spouse's Will upon death, for the benefit of the surviving non-U.S. citizen spouse. Here, assets are settled by the deceased US citizen spouse for the benefit of the surviving non-US citizen spouse. Estate tax is generally not levied immediately on the death of the US citizen spouse, but is deferred until principal distributions are made from the trust or upon the death of the surviving spouse [11]. The surviving spouse may continue to receive income from the trust during their lifetime.

Why This Matters for Indian Families: This is a common issue in cross-border Indian families where one spouse acquires US citizenship while the other does not. Without proper planning, the non-citizen surviving spouse may face an immediate estate tax bill on assets that would otherwise pass tax-free between citizen spouses.

In a nutshell…

Issue	US Citizen / US Domiciliary	Green Card Holder Living in India (Not US Domiciled)	Indian Resident (Non-US Citizen/Non-US Resident)
Assets exposed to US Estate Tax on death	Worldwide assets	Only US-situs assets (e.g., US real estate, shares of US companies)	Only US-situs assets
Estate Tax Exemption (2026)	~$15 million [12]	Only $60,000 [13]	Only $60,000
Exposure to US Gift Tax	Applies to worldwide gifts	Applies only to gifts of US real estate and other US tangible property	Applies only to gifts of US real estate and other US tangible property
Gift of US Shares / US Mutual Funds	Can trigger US gift-tax reporting rules	Generally, not subject to US gift tax	Generally, not subject to US gift tax
Annual Tax-Free Gifts (2026)	$19,000 per recipient	$19,000 per recipient (where applicable)	$19,000 per recipient (where applicable)
Tax-Free Gift to Non-US Citizen Spouse (2026)	Up to $194,000 per year	Up to $194,000 per year	Up to $194,000 per year
Transfer to Surviving Spouse on Death	Unlimited if spouse is US citizen; otherwise, special QDOT planning may be required[14]	Similar treatment for US-situs assets	Similar treatment for US-situs assets
State-Level Estate Tax	May apply depending on the state	May apply on US-situs assets located in those states	May apply on US-situs assets located in those states

Closing Remarks

> *The Sheth family shows how this works: the same family can face very different US tax outcomes. Mr. Sheth, who is neither a US citizen nor based in the US, is taxed only on his US assets, and gets an exemption of just $ 60,000. Priya, as a US citizen, is taxed on everything she owns, anywhere in the world. Karan's position depends less on his green card and more on where he has truly made his home. What matters most is a person's status, which comes down to citizenship or where they are settled, not income tax residence. And that status can change over time.*

Review the position before...

- buying US real estate or building a sizeable US-listed portfolio;
- moving into, or out of, the United States;
- surrendering a green card or US citizenship; or
- making a large gift or bequest across the US border.

For many Indian families, the exposure arises unintentionally, and the real issue is usually not complexity but lack of awareness. With timely review and proper structuring, a significant part of the exposure can often be managed in advance.

References

[1] US transfer-tax rates are graduated from 18% to 40%, but for an NRNC the unified credit ($ 13,000 under IRC § 2102(b), equivalent to a $ 60,000 exemption) absorbs only the lowest brackets, so the effective marginal rate at any meaningful estate size is 40%.

[2] Treas. Reg. § 20.0-1(b)(1). The factors typically reviewed include length and continuity of physical presence, location of the family home and personal effects, place of business and investments, voter and motor-vehicle registrations, club and religious memberships, and the individual's declared intentions.

[3] IRC § 2104(a) read with Treas. Reg. § 20.2104-1(a)(5) – situs of corporate stock follows the place of incorporation of the issuer, irrespective of where the share certificates or the brokerage account are physically located.

[4] IRC § 2105(b). Cash held in a US brokerage account, however, is generally treated as US-situs property.

[5] IRC § 2501(a)(2). The exception covers shares, bonds and similar intangibles. It does not cover US real estate or tangibles physically located in the US.

[6] IRC § 2503(b); $ 19,000 per donee for calendar year 2026. The exclusion is available irrespective of the donor's status (citizen, domiciliary or NRNC) and is per donee, per year.

[7] IRC § 2010(c). Portability is not available where the surviving spouse is a non-US citizen unless the assets pass through a QDOT.

[8] One missed FBAR or late Form 3520 can trigger covered status even if net worth is below $2 million.

[9] IRC §§ 877A and 2801. A long-term resident is a green-card holder for any part of 8 of the last 15 tax years. On surrender, a covered expatriate is subject to a mark-to-market exit tax under § 877A; in addition, every later gift or bequest from such an expatriate to a US recipient attracts a 40% transfer tax under § 2801, payable by the recipient.

[10] IRC § 2523(i); $ 194,000 for calendar year 2026 (unlike the unlimited marital deduction otherwise available between spouses who are both US citizens).

[11] IRC § 2056A. Tax is deferred – not avoided – and is collected on principal distributions from the QDOT and on the surviving spouse's death.

[12] The estate, gift and GST exemption was permanently set at $ 15 million per individual (indexed for inflation from 2027) by the One Big Beautiful Bill Act, 2025, amending IRC § 2010(c).

[13] IRC § 2102(b). Unlike the citizen exemption, the $ 60,000 figure is not indexed and has been unchanged since 1988.

[14] Qualified Domestic Trust (QDOT) – is explained briefly under section titled "Non-US Citizen Spouse Issue"

About kcmHeirloom

KCMHeirloom is a specialized publication by the Succession Planning team at K C Mehta & Co LLP Chartered Accountants, focused on inheritance planning, estate structuring, and family business governance. It explores key challenges, evolving regulations, and best practices in wealth succession, offering valuable insights for families, business owners, and trustees.

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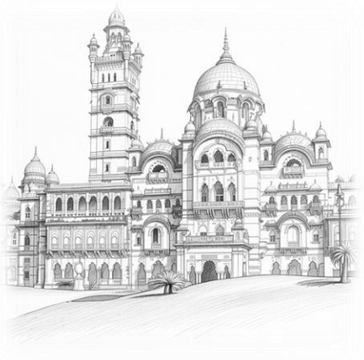
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