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Estate and Death Tax Planning for Non-Residents Owning Iowa Real Estate

by

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ESTATE AND DEATH TAX PLANNING FOR NON-RESIDENTS OWNING IOWA REAL ESTATE

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I. INTRODUCTION

Ownership of Iowa real estate by non-residents is quite widespread. Much of the Iowa real estate traditionally owned by non-residents is agricultural real estate that was previously operated by the owner who has now retired and moved from Iowa or was real estate that was inherited by "off-farm" heirs who no longer reside in Iowa. The current farm financial crisis has also caused a dramatic decrease in farm real estate values in Iowa. Consequently, due to depressed agricultural real estate values, non-resident investors who wish to capitalize on a depressed market value of agricultural real estate may increase the numbers of non-residents owning Iowa real estate. This possibility of increased non-resident ownership and the traditional non-resident ownership of Iowa real property will present increased planning opportunities for non-residents which will require attorneys and other advisors to increase their understanding of the Iowa probate laws and death tax laws applying to non-residents.

Initially this article will analyze the current Iowa death tax structure and highlight the Iowa ancillary administration requirements and procedures. This article will then suggest alternatives for decreasing the Iowa death taxes of non-residents and for avoiding formal probate requirements in appropriate situations.

II. IOWA DEATH TAXES

Iowa currently imposes both an inheritance tax¹ and an estate tax.² These taxes are designed to achieve a minimum Iowa tax equal to the federal estate tax state death tax credit.³ Due to comparable or lower state death tax rate structures in many of the contiguous states and in other states in which non-resident ownership of Iowa realty appears to be most

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1. IOWA CODE chapter 450 (1985).

2. IOWA CODE chapter 451 (1985).

3. 26 U.S.C. § 2011 (1982).

common, the estate planner will need to estimate Iowa inheritance and estate taxes for a non-resident owner of Iowa real property as well as the death taxes in the domiciliary state in order to minimize total inheritance and estate taxes.⁴ The following paragraphs provide a general outline of the Iowa death taxes so that such an estimate can be made.

A. *Property Subject to Iowa Inheritance Tax*

For a non-resident, property is subject to the Iowa inheritance tax if the property is located in Iowa, subject to the jurisdiction of the Iowa courts, or after death brought into Iowa and becomes subject to the jurisdiction of the Iowa courts. It makes no difference whether the property, or any interest in the property, is "real, personal, or mixed" or whether it is "tangible or intangible."⁵

Fortunately, the Iowa inheritance tax relating to the taxation of personal property of non-residents is governed by statute and is relatively straightforward.⁶ For non-residents, personal property, except tangible personal property located in Iowa, is not taxable in Iowa if the state of a non-resident's domicile does not tax the personal property of Iowa residents that

4. Many states impose only an estate tax, sometimes called a "gap" tax, a "sponge" tax, or a "pickup" tax, which is a state death tax on the transfer of a decedent's property equal to the amount of the federal estate tax state death credit found in 26 U.S.C. § 2011 (1982). ARIZ. REV. STAT. ANN. § 42-1521 (1986); CAL. REV. TAX. CODE § 13302 (Deering Supp. 1986); FLA. STAT. § 198.02 (1986); ILL. REV. STAT. Ch. 120, § 405.2 (Supp. 1986); MINN. STAT. § 291.03 (Supp. 1986); MO. REV. STAT. § 145.011 (Supp. 1986); TEX. TAX CODE ANN. § 211.051 (Vernon 1982). Other states impose both an inheritance tax and an estate tax. For example, South Dakota imposes both inheritance and "pickup" estate taxes to achieve the applicable federal state tax credit with inheritance tax rates greater than those in Iowa in certain instances, particularly on transfers to beneficiaries other than spouses in excess of \$15,000. S.D. COMPILED LAWS ANN. §§ 10-40-21-40-22, -40A-3 (1982). Nebraska imposes both inheritance and "pickup" estate taxes to capture the full amount allowed as a state credit under 26 U.S.C. § 2011 (1982) with inheritance tax rates generally lower than Iowa's except for transfers to non-spouse, non-relative survivors in excess of \$50,000 which are higher than Iowa's inheritance tax rates. Nebraska rates are also potentially higher than Iowa's rates for certain smaller inheritances to relatives other than the spouse. NEB. REV. STAT. §§ 77-2004-0-06, -2101.01 (1981). Wisconsin imposes both inheritance and "pickup" estate taxes with inheritance tax rates that may be lower than Iowa's in instances of smaller inheritances but higher than Iowa's non-spousal rates in excess of \$25,000 to \$50,000, depending on the class of the survivor involved. WIS. STAT. ANN. § 77.19 (1985).

5. IOWA CODE § 450.2 (1985).

6. It has been generally conceded that a state has the constitutional power to tax real estate and tangible personal property owned by a non-resident which is located in that state. However, there has been considerable dispute concerning the power of a state to tax a non-resident's personal property not located in the state and to tax the intangible personalty of a non-resident wherever located. The constitutional limitations on a state's power to tax personal property, especially intangible personal property, has a long and tangled history beyond the scope of this article. For an excellent discussion of the history and development of the law in this area, see S. KURTZ, IOWA ESTATES, §§ 23.3, 23.4 (1981). See also Comment, *Double Domicile and Federal Interpleader Revisited*, 33 S.W.L.J. 1241 (1980).

is not located in that foreign state, or if the state of the non-resident's domicile has a reciprocal provision that would not tax the personal property of Iowa residents that is not located in that state.⁷ The property law of the state of the situs determines the classification of property, including a determination of whether property is classified as tangible or intangible.⁸ Intangible personal property generally includes such items as a vendor's interest in a real estate contract, stocks, bonds, bank accounts, and certificates of deposit.⁹

The gross estate for Iowa inheritance tax purposes includes gift transfers made within three years of death to the extent the transfers are in excess of the annual gift tax exclusion allowable for each donee under section 2503 of the Internal Revenue Code;¹⁰ transfers taking effect at death including transfers which involve a retained life estate or interest;¹¹ and property owned in joint tenancy with rights of survivorship to the extent that contribution can be traced to the decedent, except that spousal joint tenancy property is presumed to be included in the taxable estate only to the extent of one-half the value.¹² Insurance proceeds paid to a named beneficiary are not subject to the Iowa inheritance tax.¹³ Property subject to a power of appointment, either general or special, is not currently subject to Iowa inheritance tax unless the power is exercised in favor of beneficiaries other than the takers in default of exercise.¹⁴ However, for decedents dying on or after January 1, 1988, property subject to a general power of appointment will be subject to the Iowa inheritance tax even if the general power is not exercised.¹⁵

Iowa law permits the reduction of the taxable estate of a non-resident for Iowa inheritance tax purposes for "liabilities," which include certain debts and costs of administration that are specifically enumerated by statute.¹⁶ The definition of "debts" for Iowa inheritance tax purposes is broader than the definition of "debts" owed by the decedent at death and varies

7. IOWA CODE § 450.91 (1985); IOWA ADMIN. CODE § 730-86.5(4) (1981). Care needs to be taken to determine what states have reciprocity statutes. As many states repeal their inheritance tax in favor of an estate or "pickup" tax based upon the federal estate tax state death tax credit, many states have repealed their reciprocal provisions not taxing the personal property of Iowa residents that is not located in that state.

8. *Dieleman's Estate v. Department of Revenue*, 222 N.W.2d 459 (Iowa 1974). IOWA ADMIN. CODE § 730-86.5(5) (1981).

9. 42 AM. JUR. 2d *Inheritance, Estate, and Gift Taxes* §§ 176-88 (1969 & Supp. 1986).

10. IOWA CODE § 450.2(2) (1985). See also IOWA ADMIN. CODE § 730-86.5(7)(d) (1985).

11. IOWA CODE § 450.2(3) (1985). See also IOWA ADMIN. CODE § 730-86.5(9) (1981).

12. IOWA CODE § 450.2(5) (1985); IOWA ADMIN. CODE § 730-86.5(8) (1981). See also *In re English's Estate*, 206 N.W.2d 305 (Iowa 1973).

13. *In re Estate of Brown*, 205 N.W.2d 925 (Iowa 1973). See also IOWA ADMIN. CODE § 730-86.5(6) (1981).

14. IOWA CODE § 450.2(4) (1985). See also IOWA ADMIN. CODE § 730-86.5(10) (1981).

15. 1985 Iowa Acts, ch. 148, § 10.

16. IOWA CODE § 450.12(1) (1985).

from the deductions available for federal estate tax purposes. For example, liabilities of a non-resident may be (i) deductible in full, (ii) not deductible, or (iii) deductible on a pro rata basis. For decedents dying after July 1, 1983, if the gross estate of any decedent, resident or non-resident, includes property with a situs outside of Iowa, the liabilities, debts and expenses must be prorated on the basis that the gross value of Iowa situs property bears to the total gross estate. However, a liability secured by a lien on property shall be allocated to the state where the property is located and shall not be prorated except to the extent the liability exceeds the value of the property.¹⁷ A liability secured by property not included in the gross estate is not deductible.¹⁸

The amount of a liability that is deductible is computed by multiplying the total amount of unsecured liabilities by a fraction of which Iowa situs property in the "gross estate" is the numerator and the total "gross estate" is the denominator.¹⁹ "Gross estate" means the gross estate for federal estate tax purposes.²⁰ If this formula produces a grossly distorted result a different formula may be used by either the Iowa Department of Revenue or the taxpayer "subject to the approval of the department."²¹

Liabilities that must be prorated include:

- (1) Court costs, both foreign and domestic
- (2) All unsecured debts
- (3) Federal and state income tax (including tax on decedent's final return), federal estate, gift, and excise tax
- (4) Expenses of funeral and burial
- (5) Support allowances
- (6) Appraisal expenses
- (7) Attorney and personal representative fees
- (8) Costs of selling personal and real property
- (9) Bond fees²²

B. Rates and Exemptions

Iowa inheritance tax rates vary with the amount of the property received and by the degree of relationship of the recipient.²³ Exemptions exist for certain recipients.²⁴ These rates and exemptions are contained in a generalized summary found at the conclusion of this article.

Rates and exemptions for non-residents are not reduced proportionally

17. IOWA CODE § 450.12(2) (1985).

18. IOWA CODE § 450.12(3) (1985).

19. IOWA ADMIN. CODE § 730-86(4)(c) (1984).

20. *Id.*

21. IOWA ADMIN. CODE § 730-86.6(4) (1984).

22. IOWA ADMIN. CODE § 730-86.6(4)(c) (1984).

23. IOWA CODE § 450.10 (1985).

24. IOWA CODE § 450.9 (1985).

for property not taxable in Iowa. For example, a surviving spouse of a non-resident is entitled to the full \$180,000 surviving spouse's exemption regardless of the percentage of the gross estate taxable in Iowa.²⁵ Because there is no proportional reduction for non-residents it may be advantageous in many situations to allow a portion of a non-resident's property to remain taxable in Iowa because it would incur little or no Iowa inheritance tax but would be taxed at higher rates in the domiciliary state.

Iowa has also adopted a marital deduction credit which began to phase in for decedent's dying on or after January 1, 1986.²⁶ The availability of a full marital deduction credit may also lessen the need to remove property from the taxable estate subject to Iowa inheritance tax.

C. Iowa Estate Tax - Chapter 451

Iowa also imposes an estate tax which is a death tax on the transfer of property. The tax is equal to the amount of the federal estate tax state death tax credit.²⁷ The formula for determining the Iowa estate tax for a non-resident is expressed as follows, with the "Iowa Estate Tax" being the unknown:

$$Y = \text{Iowa Estate Tax}$$

$$Y = \text{State Death Tax Credit} \times \frac{\text{§ 2011 Property Taxable in Iowa}}{\text{Federal Gross Estate}}$$

The Iowa estate tax is imposed only if and to the extent the federal estate tax exceeds the Iowa inheritance tax.²⁸ An important distinction exists between the two Iowa death taxes due to the fact that the Iowa estate tax is a charge against the estate.²⁹ As a charge, the Iowa estate tax is generally payable from the residue of the estate.³⁰ In contrast, the Iowa inheritance tax is not a charge, but is generally a reduction in a beneficiary's share and generally is not paid from the residue by the estate in the absence of a specific direction in the decedent's will.³¹

III. BASIC ANCILLARY ADMINISTRATION

A. Admitting the Will to Probate

A will originally probated in another state or country may be admitted

25. *See id.*

26. IOWA CODE § 450.10(7) (1985).

27. 26 U.S.C. § 2011 (1982).

28. IOWA CODE § 451.2 (1985).

29. IOWA CODE § 633.3(4) (1985).

30. IOWA CODE §§ 633.436-.437, .449 (1985).

31. IOWA CODE § 450.5 (1985).

to probate in Iowa by filing a copy of the will and a copy of the original record of probate with the Iowa court. The copies must be authenticated by the certificate of the clerk of the foreign court and must be under seal, if the clerk has a seal. If there is no clerk of the foreign court, then the copies must be authenticated by the certificate of the judge of the foreign court and must be under seal, if the judge has a seal.³²

Original jurisdiction for probate may be in any county where the non-resident's property was located.³³ If more than one county would have jurisdiction, the county in which proceedings are first commenced retains jurisdiction.³⁴ If there is real estate in more than one county, it will be necessary to certify the relevant portion of the probate proceedings to all other counties where the real estate is located.³⁵

The authenticated copies of the will and the original record of probate are presented to the court by application and the application is usually made by the foreign personal representative. This application generally is combined with the application to appoint an executor for the Iowa administration which is discussed in the following paragraphs.

B. *Appointment of Executor*

A foreign executor or personal representative may apply to be appointed as the executor for the Iowa administration after qualifying in the domiciliary proceeding. A resident Iowa executor must be appointed to serve with the non-resident executor unless the court "for good cause shown" permits the non-resident to serve alone.³⁶ "Good cause" is not defined in the statute nor by case law, and appears to be discretionary with the court. Generally, it is easier to qualify a non-resident to act as the sole executor if the non-resident is nominated in the will, if the non-resident is a family member, if the non-resident is a significant beneficiary, and if the bulk of the estate subject to administration in Iowa is real estate.

Non-resident natural persons are legally permitted to serve in a fiduciary capacity in Iowa if they meet the qualifications required for Iowa natural persons and the court permits them to serve.³⁷ Non-resident banks and trust companies are permitted to serve in a fiduciary capacity in Iowa if Iowa banks and trust companies can serve in the foreign state.³⁸ Most states have reciprocity statutes that would permit an Iowa bank or trust company to serve in a fiduciary capacity in the foreign state, so this is seldom a problem.

The application for appointment must contain the name and address of

32. IOWA CODE § 633.496 (1985).

33. IOWA CODE § 633.12 (1985).

34. IOWA CODE § 633.14 (1985).

35. IOWA CODE § 633.48 (1985).

36. IOWA CODE § 633.502 (1985).

37. IOWA CODE §§ 633.63, .64(1) (1985).

38. IOWA CODE § 633.64(2) (1985).

the foreign personal representative and the name and address of the resident personal representative. If no resident personal representative is to be appointed, the application must include the reasons why no Iowa personal representative need be appointed. The application must also be accompanied by a certificate of the foreign court granting the letters testamentary.³⁹ Generally these letters of appointment will be included in the authenticated copy of the original record of probate.

By qualifying as an executor, the non-resident executor submits himself to the jurisdiction of the court, agrees that all property coming into his hands is subject to the Iowa court's jurisdiction, agrees to be subject to all orders of the court, agrees to the jurisdiction of the Iowa courts in all actions and proceedings resulting from his fiduciary relationship, and appoints the clerk of the Iowa District Court as his lawful attorney and resident agent for service of process.⁴⁰ Service upon a non-resident executor may be made by delivering or mailing the notice or process to the clerk.⁴¹

C. Intestacy

Commencing an intestate administration is quite similar to the appointment of an executor and probating a foreign will. The foreign personal representative, after qualifying in the domiciliary state, may apply for appointment in Iowa but only before another personal representative has been appointed. A resident co-personal representative must be appointed unless the court "for good cause shown" permits the non-resident to serve alone.⁴² "Good cause" qualification of a non-resident as a personal representative, and provisions applying to the personal representative were discussed above. Original jurisdiction for probate may be in any county where the non-resident decedent's property was located and jurisdiction once commenced in a county is retained.⁴³

The application for appointment must contain the name and address of the foreign personal representative and the name and address of any resident co-personal representative. If no resident personal representative is to be appointed, the application must include the reason why no Iowa personal representative should be appointed. The application must also be accompanied by a certificate of the clerk of the foreign court granting the letters testamentary.⁴⁴

39. IOWA CODE § 633.503 (1985).

40. IOWA CODE § 633.71 (1985).

41. IOWA CODE § 633.72 (1985).

42. IOWA CODE § 633.500 (1985). See *supra* note 36 and accompanying text.

43. IOWA CODE §§ 633.12, .14 (1985).

44. IOWA CODE § 633.501 (1985).

D. *Basic Administration and Distribution*

All provisions of Iowa probate law, unless expressly providing otherwise, apply to the administration of a non-resident estate, whether testate or intestate. All provisions of Iowa law, unless expressly providing otherwise, also apply to the powers, duties and responsibilities of the personal representative, whether a resident or a non-resident.⁴⁵

For non-resident estates under ancillary administration in Iowa, the court may require payment of all claims filed and allowed for Iowa residents and satisfaction of all legacies and distributive shares due Iowa residents before allowing estate property to be removed from Iowa.⁴⁶ Fees for attorneys and executors are limited by statute to a maximum fee for an ordinary administration with both fees equal to six percent (6%) of the first \$1,000 of the estate subject to Iowa inheritance tax, four percent (4%) of the next \$4,000 of the estate subject to Iowa inheritance tax, and two percent (2%) of the remaining estate subject to Iowa inheritance tax.⁴⁷ Extraordinary fees may be awarded by the court for extraordinary services which, by statute, include certain tax matters, litigation, and real estate matters.⁴⁸ Court costs, which vary with the size and composition of the estate, must also be paid.⁴⁹

E. *Nondomiciliary Original Probate*

Iowa law allows the will of a non-resident to be admitted to original probate in a county in Iowa where the decedent's personal or real property was located if there is no domiciliary administration.⁵⁰ This procedure would be used in those situations where no domiciliary probate is required because there are no or few assets in the domiciliary state or where a procedure similar to Iowa's clearance from inheritance tax procedure (hereinafter referred to as Iowa's C.I.T. procedure)⁵¹ is available in the domiciliary state. The original will is offered for probate and the procedure for probate is virtually identical to a normal probate procedure for an Iowa resident.

F. *Alternatives to Formal Probate*

There are several alternatives to formal probate that involve non-probate transfers of joint tenancy property or property held in trust. The clearance from inheritance tax procedure (short-form probate or C.I.T.) which is commonly used for Iowa residents is also available for non-residents with

45. IOWA CODE §§ 633.88, .498 (1985).

46. IOWA CODE § 633.504 (1985).

47. IOWA CODE §§ 633.197-198 (1985).

48. IOWA CODE § 633.199 (1985).

49. IOWA CODE § 633.31 (1985).

50. IOWA CODE § 633.495 (1985).

51. IOWA CODE § 450.22 (1985).

property, especially real estate, located in Iowa.⁵² A Report and Inventory must be filed with the district court in the county where any real estate is located and an inheritance tax return is required. However, if the Iowa inheritance tax lien has expired because of the passage of more than twenty years since the decedent's death, then a C.I.T. filing is not needed.⁵³

Another alternative to formal probate is to utilize the foreign will as a muniment of title. If real property, or any interest in real property, is owned outright by a non-resident who died testate and there is no likelihood of sale, mortgage or transfer within five years of death, then more than five years after death an exemplified copy of the the foreign will and the order admitting that will to probate in the foreign state may be recorded in the Iowa county in which the non-resident's real estate is located if the will has not previously been admitted nor denied probate in Iowa. The will disposes of the property as though the will had been admitted to probate in Iowa.⁵⁴ All claims are barred five years after the date of death.⁵⁵

In a procedure similar to recording a foreign probated will after five years, the heirs of an intestate decedent may establish ownership after five years by affidavit if no present administration was opened in Iowa within five years after death. All claims are barred five years after the death of the decedent, but a C.I.T. is necessary unless the death occurred more than twenty years earlier.⁵⁶

IV. PLANNING ALTERNATIVES AND CONSIDERATIONS

In regard to tax and estate planning for the non-resident, it is generally fairly easy to remove Iowa real estate from the imposition of the Iowa death taxes and from the need for formal probate administration by disposing of the property or by converting the real estate to intangible personal property. However, the removal of property from Iowa taxation is not always desirable if the result is to increase death taxes in the domiciliary state by more than the savings in Iowa taxes and administration costs or if the result is to forego an increase in basis which may result in higher income taxes upon the eventual disposition of the property by the recipient of a gift. Thus there should be an initial determination of the state death taxes and administration costs for both the domiciliary state and for Iowa with a comparison of the post-planning taxes and costs before any of the alternatives are implemented.

52. *Id.*

53. IOWA CODE § 450.7 (1985). *See also* IOWA LAND TITLE STANDARDS § 4.4 (6th ed. 1985).

54. IOWA CODE § 633.497 (1985).

55. IOWA CODE § 633.413 (1985).

56. *Id.* *See also* IOWA LAND TITLE STANDARDS § 9.8 (6th ed. 1985).

A. Gift of Property

The most obvious method of removing the property from probate administration and death taxation in Iowa is to transfer the property *inter vivos* by gift. Although Iowa has no gift tax, the non-resident donor must take into account the consequences of the federal gift tax.⁵⁷ The gross estate for Iowa inheritance tax and estate tax purposes includes gifts and transfers without full and adequate consideration made within three years of death. Any such transfer is taxable to the extent that the value of the gift or transfer exceeds the \$10,000 present interest exclusion found in section 2503 of the federal gift tax.⁵⁸

B. Revocable Trust

A transfer of real estate to a revocable trust does not change an interest in real estate to intangible personal property thereby avoiding Iowa taxation, but the transfer to a revocable trust will avoid a formal probate of the estate for the purpose of transferring title. Under this alternative, the non-resident grantor may retain almost total control over the real estate because of the right to revoke the trust at any time and may also appoint himself as the trustee or one of the trustees of the trust.

Until such time as the real estate is sold, mortgaged or transferred by the trust, Iowa law does not require that the trust document be recorded in the county in which the real estate is located. At the time the property is sold, mortgaged or transferred, the purchaser, mortgagee or transferee should require a showing of the trustee's authority to undertake the proposed action. At that time, there is a possibility that the entire trust document will have to be recorded, although, the necessary authority for the intended action can be shown by an affidavit from the trustee setting forth the appropriate trust provisions authorizing the action by the trustee.⁵⁹

Upon the death of the non-resident grantor, the trust retains title to the real estate, and no formal probate proceedings are necessary to clear the title to the real estate. However, a C.I.T. procedure is necessary to show the clearance of Iowa inheritance taxes on the property, since the non-resident grantor retained the ability to revoke the trust during his life.⁶⁰ If the trust were not revocable by the non-resident grantor, no C.I.T. procedure would be required.

If the real estate is to be transferred to a trust, the planner should be

57. 16 U.S.C. § 2501 (1982).

58. *See supra* note 10.

59. IOWA LAND TITLE STANDARDS § 4.8 (6th ed. 1985). *See also* *Zion Church v. Parker*, 114 Iowa 1, 86 N.W. 60 (1901); *Boardman v. Willard*, 73 Iowa 20, 34 N.W. 487 (1887); *Sleeper v. Iselin*, 62 Iowa 583, 17 N.W. 922 (1883); R. PATTON & C. PATTON, *LAND TITLES* § 228 (2d ed. 1957).

60. IOWA CODE § 450.3(3) (1985).

aware that there are restrictions on the ownership of "agricultural land" by certain trusts under Iowa law.⁶¹ Generally, because the likely beneficiaries of such a trust will qualify the trust to own farmland, these restrictions should not prevent the transfer of the real estate to a revocable trust.

C. *Reserved Life Estate*

Similar in concept to the transfer to a revocable trust, a non-resident owner of Iowa real estate may make any outright transfer of the real estate to his intended beneficiaries and retain a life estate. Upon the death of the person retaining the life estate, there is no need for formal probate to transfer the title to the real estate, since the life estate holder's interest on the real estate automatically terminates. To establish merchantable title to the real estate in the remainderman, the only requirements are to show the death of the life estate holder, and since the life estate is a retained life estate, a clearance of Iowa inheritance tax.⁶² The obvious disadvantage of the retained life estate, in comparison with the revocable trust, is that the grantor, solely by his own actions, cannot regain fee title to the real estate.

D. *Joint Tenancy with Rights of Survivorship*

Iowa law recognizes a joint tenancy with rights of survivorship.⁶³ Trans-

61. If the real estate is "agricultural land" only a "family trust," "authorized trust" or "testamentary trust" may own farmland. IOWA CODE § 172C.4 (1985). A "family trust" is a trust in which a majority interest is held by and the majority of beneficiaries are persons related to each other as spouse, parent, grandparent, lineal ascendants or descendants of grandparents or their spouses, or persons acting in a fiduciary capacity for persons so related, and all beneficiaries are natural persons, who are not acting as a trustee or persons acting in a fiduciary capacity or nonprofit corporations. IOWA CODE § 172C.1(11) (1985). "Authorized Trust" means a trust other than a family trust in which the beneficiaries do not exceed 25 and beneficiaries are natural persons (not as trustee) fiduciaries or nonprofit corporations. IOWA CODE § 172C.1(12) (1985). "Testamentary Trust" means a trust created by devising or bequeathing property in a trust in a will. IOWA CODE § 172C.1(13) (1985).

62. IOWA CODE § 450.3(3) (1985).

63. To create joint tenancy ownership of Iowa real estate, the property must be held in joint tenancy with rights of survivorship instead of as tenants in common which does not include rights of survivorship. Unless specific language is included in the document of conveyance to establish the joint tenancy, conveyances to two or more individuals create a tenancy in common. IOWA CODE § 557.15 (1985). In order to avoid a tenancy in common and establish a joint tenancy in real property, a contrary intent to creating a tenancy in common must be expressed in the document. For a general discussion of the words necessary to create a joint tenancy with full rights of survivorship, see 20 AM. JUR. 2D *Cotenancy and Joint Ownership* §§ 17, 44 (1965). Iowa courts have upheld various granting clauses as establishing a joint tenancy with rights of survivorship. See *Hoffman v. Stigers*, 28 Iowa 302 (1869); *Wood v. Logue*, 167 Iowa 436, 149 N.W. 613 (1914); *In re Estate of Miller*, 248 Iowa 19, 22, 79 N.W.2d 315, 319 (1956) (a conveyance to A or B, or the survivor thereof created a joint tenancy with right of survivorship). The authors prefer the following language: "A and B as joint tenants with full right of survivorship, and not as tenants in common." However, Iowa courts have accepted lesser language when they have been able to determine that the intent of the parties was to

ferring property into joint tenancy with rights of survivorship does not avoid Iowa death taxes, although the creation of joint tenancy avoids the need for formal probate which may greatly lessen the cost of administration.⁶⁴ Property held in joint tenancy with a spouse is accorded more favorable Iowa tax treatment because one-half the value of the property is excluded from the coverage of the Iowa death taxes and a greater portion may be excluded if the surviving spouse can prove that he or she contributed more than one-half of the consideration. Property held as joint tenants with a person other than a spouse is subject to Iowa taxes except to the extent the survivor can prove his or her contribution.⁶⁵

If a non-resident owned real property in joint tenancy with another individual or individuals, upon the death of the non-resident, his interest in the real property is automatically transferred to the surviving joint tenants by operation of law.⁶⁶ Therefore, no administration of the estate is necessary.⁶⁷ Only a showing of the death certificate or an affidavit establishing the death of the deceased joint tenant, and the filing of a clearance of inheritance tax proceeding and the payment of any inheritance tax are necessary. If the non-resident joint tenant has been dead for more than twenty years, the inheritance tax lien against the real estate has lapsed, and no C.I.T. need be filed.⁶⁸ It is not necessary to show non-liability of the estate of the non-resident for federal estate tax since the federal estate tax is not a lien against real estate held in joint tenancy.⁶⁹

E. *Transfer of Property to a Corporation or Partnership*

Other planning alternatives involve converting Iowa real estate into intangible personal property to reduce Iowa death taxes. The most common methods are to transfer the real estate (and also tangible personal property) to a corporation or a partnership.

Real property owned by an individual may be transferred to either a general or limited partnership. Iowa has adopted the Uniform Partnership Act⁷⁰ and the Uniform Limited Partnership Act.⁷¹ "A [general] partnership is an association of two or more persons to carry on as co-owners of a business for profit."⁷² "A limited partnership is defined as a partnership formed by two or more persons under the laws of [Iowa] and having one or more

establish a joint tenancy and not a tenancy in common. *See id.*

64. IOWA LAND TITLE STANDARDS (6th ed. 1985) § 9.9.

65. IOWA CODE § 450.3(5) (1985).

66. *Fleming v. Fleming*, 194 Iowa 71, 88-89, 174 N.W. 946, 953 (1919).

67. IOWA LAND TITLE STANDARDS (6th ed. 1985) § 9.9; IOWA CODE § 450.22 (1985).

68. IOWA CODE § 450.7(1)(a) (1985).

69. Rev. Rul. 56-144, 1956-1 C.B. 563.

70. IOWA CODE chapter 544 (1985).

71. IOWA CODE chapter 545 (1985).

72. IOWA CODE § 544.6(1) (1985).

general partners and one or more limited partners."⁷³

Either type of partnership may acquire any estate in real property in the partnership name.⁷⁴ For example, a non-resident might transfer real estate to a partnership in which the intended beneficiaries of his estate are also named as partners. Control of the operation and the sale of the real estate can be retained by the transferor either through control provisions in the partnership agreement, or in a limited partnership by the non-resident appointing himself the general partner, and making everyone else limited partners.⁷⁵

After the real property has been conveyed to a partnership, the non-resident does not have an interest in real estate to be included in his estate. Only the partnership interest, which is intangible personal property, is included in his estate.⁷⁶

A general partnership agreement does not need to be filed or recorded. Iowa law requires a partnership to file a trade name certificate with the recorder of the county where the business is to be conducted by the partnership setting forth the name, post office address, and residence address of each person having an interest in the partnership, and the address of where the business is to be conducted.⁷⁷ For each day such a statement is not filed, a person violating the provision is guilty of a simple misdemeanor.⁷⁸ An Iowa limited partnership must file this Certificate of Limited Partnership with the Secretary of State and the County Recorder in the county in which the office of the limited partnership is located.⁷⁹

A foreign limited partnership may also own Iowa real estate. Before transacting business in Iowa, it must register as a foreign limited partner-

73. IOWA CODE § 545.101(7) (1985).

74. IOWA CODE §§ 544.8(3), 545.106 (1985).

75. Once the real estate has been transferred to a partnership, the real property may be conveyed by one or any number of the general partners on behalf of the partnership. Iowa partnership law assumes each general partner may convey the entire interest of the partnership in real property. Unless a bona fide purchaser has knowledge that a partner does not have authority to transfer the property, if property is conveyed by a partner, the partnership will not be able to recover the real property from the third party. IOWA CODE §§ 544.10(1), 545.403 (1985). If a general partner is concerned with any other general partner transferring real property owned by the partnership without approval of the partnership or if one partner wants to retain control of the right to transfer the real estate, he should file a memorandum of partnership in the land records of the county where the real property is located setting forth the necessary partnership action and who can sign deeds on behalf of the partnership to give constructive notice to third parties. If the real estate is in the same county where the office of the limited partnership is located, this recording is automatically completed since the Certificate of Limited Partnership is recorded with the Secretary of State and the County Recorder of the county where the office of the limited partnership is located. IOWA CODE § 545.206 (1985).

76. IOWA CODE §§ 544.26, 545.701 (1985).

77. IOWA CODE § 547.1 (1985).

78. IOWA CODE § 547.4-5 (1985).

79. IOWA CODE § 545.201(1) (1985) (Iowa limited partnership) or IOWA CODE § 545.902 (1985).

ship with the Iowa Secretary of State's office.⁸⁰ Failure to register does not impair the validity of actions taken by the foreign limited partnership in Iowa.⁸¹ Until the foreign partnership is registered in Iowa, however, it is denied certain rights under Iowa law.⁸²

A non-resident individual may also transfer real estate to a corporation to avoid the need to probate an estate in Iowa and to reduce or avoid Iowa death taxes. An Iowa corporation is authorized to "acquire, own, hold, improve, use or otherwise deal in and with, real or personal property."⁸³

If the corporation owning the real estate is not an Iowa corporation, the corporation must be admitted as a foreign corporation under the Iowa law.⁸⁴ A foreign corporation must continuously maintain a registered office and appoint a registered agent within the State of Iowa.⁸⁵ If the real estate to be transferred to a corporation is "agricultural land," as defined in the Corporate or Partnership Farming statute,⁸⁶ the corporation must qualify as an "authorized farm corporation" or a "family farm corporation."⁸⁷

The alternative of transferring real property to a corporation must be evaluated not only for the benefit of avoiding probate in Iowa and reducing the Iowa death taxes, but must also consider the income tax consequences to the non-resident. If the corporation has taxable income, there may be in-

80. IOWA CODE § 545.902 (1985).

81. IOWA CODE § 545.907(2) (1985).

82. IOWA CODE § 545.907 (1985).

83. IOWA CODE § 496A.3(4) (1985).

84. IOWA CODE § 496A.103(1) (1985). See IOWA CODE § 496A.107 (1985) for the requirements for registering a foreign corporation in Iowa.

85. IOWA CODE § 496A.110 (1985).

86. IOWA CODE chapter 172C (1985).

87. "Family Farm Corporation" is defined as:

a corporation: a) [f]ounded for the purpose of farming and the ownership of agricultural land in which a majority of the voting stock is held by and the majority of the stockholders are persons related to each other as spouse, parent, grandparent, lineal ascendants of grandparents or their spouses and other lineal descendants of the grandparents or their spouses, or persons acting in a fiduciary capacity for persons so related; b) [a]ll of its stockholders are natural persons or persons acting in a fiduciary capacity for the benefit of natural persons or family trusts . . . ; and c) [s]ixty percent of the gross revenues of the corporation over the last consecutive three-year period comes from farming.

IOWA CODE § 172C.1(8) (1985).

'Authorized Farm Corporation' means a corporation other than a family farm corporation founded for the purpose of farming and the ownership of agricultural land in which: a) [t]he stockholders do not exceed twenty-five in number; and b) [t]he stockholders are all natural persons or persons acting in a fiduciary capacity for the benefit of natural persons or non-profit corporations.

IOWA CODE § 172C.1(9)(a) (1985). "Agricultural Land" means land suitable for use in agriculture. IOWA CODE § 172C.1(5) (1985). Under the normal factual situations when an individual would be transferring real estate to a corporation to avoid the need to probate the estate in Iowa, the individual should be able to structure a corporation to qualify as owning farmland in the state of Iowa.

come tax paid at the corporate level, as well as the shareholder may pay tax for any dividends received from the corporation, or upon its liquidation. Corporate ownership of real estate may be more attractive if the corporation can qualify for tax treatment as an S corporation, since the tax consequences of ownership by the corporation flow through to the individual.⁸⁸

The use of a corporation to convert the realty to personalty, as opposed to using a partnership for such transformation, provides the advantage that the real estate does not need to be used in a business operated for profit to be held by a corporation. Also, there only needs to be one stockholder in a corporation while the Uniform Partnership Act and Uniform Limited Partnership Act require two or more partners. However, the disadvantages are the possibility of increased taxes, possible restrictions on the number or identity of shareholders, the requirement to maintain a registered office and registered agent, and the payment of corporate annual fees to the State of Iowa.

V. CONCLUSION

In summary, estate and tax planning for the non-resident owning Iowa real estate requires a summary knowledge of Iowa death taxes and probate procedure and a careful analysis and comparison of the death taxes and costs in Iowa and in the domiciliary state. Iowa law allows for a variety of planning alternatives for ownership of Iowa real estate to help accomplish the objectives of a non-resident's estate plan.⁸⁹

88. For a further discussion of the use of a corporation for estate planning, see E. HOOD, S. KURTZ, J. SHORS, *CLOSELY HELD CORPORATIONS IN BUSINESS AND ESTATE PLANNING* (1982).

89. The following is a summary of Iowa Inheritance Tax Rates and Exemptions:

Exemptions

Widow or Widower - \$180,000
 1988 - full marital credit
 Child - \$50,000
 Parent and Other Lineal Descendant - \$15,000

Rates

<u>Amount Taxable</u>	<u>Class 1 Beneficiaries</u>	<u>Class 2 Beneficiaries</u>	<u>Class 3 Beneficiaries</u>
0 - \$5,000	1%	5%	10%
\$ 5,000 - \$12,000	2%	5%	10%
\$12,500 - \$25,000	3%	6%	10%
\$25,000 - \$50,000	4%	7%	10%
\$50,000 - \$75,000	5%	7%	12%
\$75,000 - \$100,000	6%	8%	12%
\$100,000 - \$150,000	7%	9%	15%
excess of \$150,000	8%	10%	15%

Class 1 Beneficiaries - Spouse, Parent, Child, Lineal Descendant

Class 2 Beneficiaries - Brother or Sister, Son-in-law or Daughter-in-law, Stepchildren

Class 3 Beneficiaries - All other individuals not in Classes 1 or 2