

# CANADA-U.S. TAX PLANNING FOR INDIVIDUALS

## Selected Tax Issues

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## Outline

- Canadian Tax System
- Canadian persons with U.S. beneficiaries
- U.S. persons with Canadian beneficiaries
- Canadians holding U.S. situs assets
- U.S. persons holding Canadian assets
- Canadians moving to U.S.
- U.S. persons moving to Canada
- U.S. citizens living in Canada

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## Canadian Tax System

	Canada	U.S.
Residency	Ties Presence	Presence Green card Citizen
Treaty	Treaty overrides domestic law Normally followed by provinces	Treaty overrides except citizen Not binding on states Last in time rule
Treaty Scope	Income tax	Income tax and estate tax not gift tax
Gift	FMV sale FMV basis (no gift tax)	Gift tax Donor's basis + gift tax

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## Canadian Tax System

	Canada	U.S.
Death	FMV sale FMV basis No estate tax	Estate tax FMV basis
Arrival	FMV basis step up or down	Historic basis but step up where Canadian deemed disposition on moving to U.S. (by Treaty)
Departure	FMV sale of most property	No implications unless expatriation
Spousal rollover	Yes, no capital gain	Yes to citizen or QDOT
Estate freeze permitted	Yes, usually corporate with frozen preferred shares	Yes, usually with grantor trust and incomplete gift or self transfer

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## Canadian Tax System

	Canada	U.S.
U.S. LLC	Foreign corporation	Flow through entity
Canadian ULC	Canadian corporation	Flow through entity
Tax rates personal	Graduated to 50%	Graduated to 48%
Tax rates corporate	25%	40%

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## Canadian Tax System

### Status of a Trust

Resident (trustee in Canada)

Deemed resident

Non-resident (default)

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## Canadian Tax System

### Non-Resident Trust

Old rules (2007)

Non-resident trust deemed resident if:

- a) Canadian resident contributor
- AND
- b) Related Canadian resident beneficiary

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## Canadian Tax System

### Non-Resident Trust

New rules (2007 onwards)

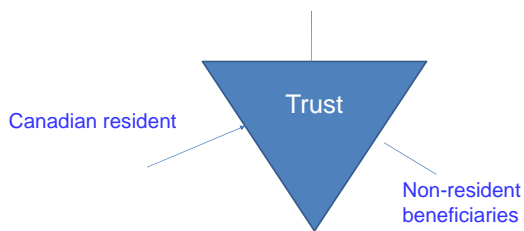
Non-resident trust deemed resident if:

Canadian resident contributor  
(irrespective of who beneficiaries are)

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## Canadian Tax System

Non-Resident



Pre 2007 – not deemed resident in Canada

2007 and after – deemed resident in Canada and taxable

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## Canadian Tax System

### Immigrant Trust

Exemption from trust being deemed resident if Canadian resident contributor not resident 60 months.

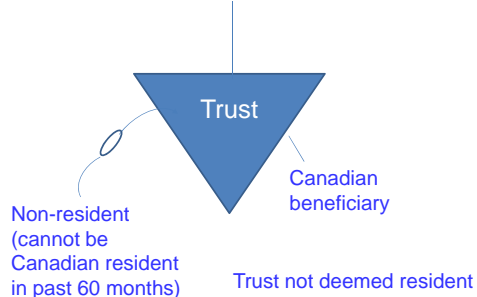
Withdrawn February 11, 2014.

Existing trusts deemed resident January 1, 2015 (except if contribution after February 11, 2014 in which case January 1, 2014).

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## Canadian Tax System

Non-Resident  
Trustee



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## Canadian Tax System

### Non-Resident Trust

- Trust not taxable except on certain Canadian source income
- Trust distributions to Canadian beneficiary
  - Taxable – if income
  - Tax-free – if capital
- No U.S. style UNI rules

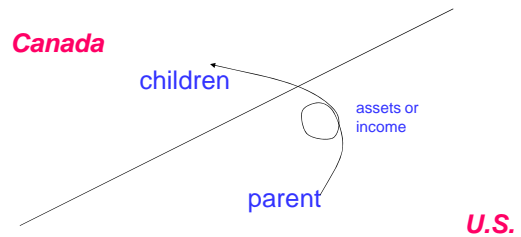
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## U.S. Persons, Canadian Beneficiaries

U.S. family wishes to benefit Canadian persons (family members in Canada)  
How to best do this?

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## U.S. Persons, Canadian Beneficiaries



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## U.S. Persons, Canadian Beneficiaries

- Gift during life v. on death
- Leave direct or to a trust
- Which assets to leave

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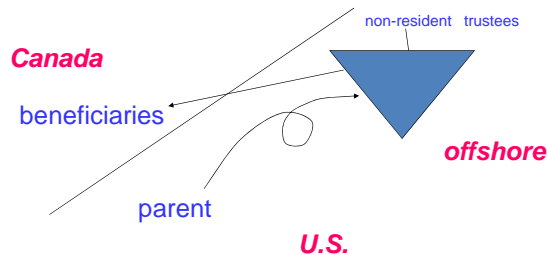
## U.S. Persons, Canadian Beneficiaries

### Canadian Implications

- Canadian resident obtains FMV basis for assets gifted or left by Will
- But taxable on future income and gains
- Consider use of non-resident trust

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## U.S. Persons, Canadian Beneficiaries



No tax to the trust  
No tax to Canadian beneficiaries on capital distributions  
Permanent tax exemption

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## U.S. Persons, Canadian Beneficiaries

### U.S. Issues

- Gift to trust or beneficiaries inter vivos → U.S. gift tax
  - Assets left by Will → U.S. estate tax
- Possibly no real difference. (Give early give often.)

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## U.S. Persons, Canadian Beneficiaries

### Which Assets?

- Preferably assets where income does not attract U.S. tax
- Good assets - cash/investments
- Bad assets - U.S. business assets  
- U.S. real estate

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## U.S. Persons, Canadian Beneficiaries

- Canadian family wishes to benefit U.S. persons (say children)
- Do during life or on death?
- Gift or bequest/direct or through a trust?
- Trust resident in Canada/U.S./offshore?

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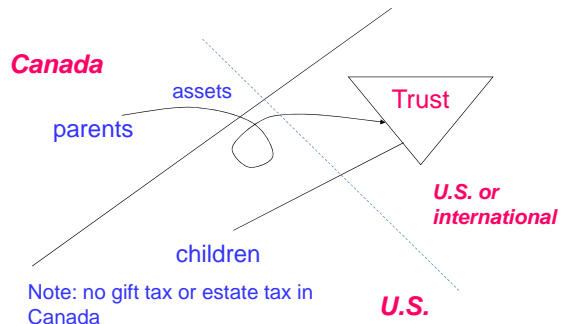
## Canadian Persons, U.S. Beneficiaries

### Objectives

Canada	U.S.
Divest income and future capital gains to non-residents	Insulation from U.S. estate taxes
	Pay no income tax on income and gains

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## Canadian Persons, U.S. Beneficiaries



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## Canadian Persons, U.S. Beneficiaries

- Trust is deemed Canadian resident while parents (contributors) are alive and taxable
- On death, Trust becomes non-resident (but only if no Canadian resident beneficiary) but has capital gain on assets owned at that time
- Possible mismatch of tax (Canada and U.S.)
- U.S. UNI rules to consider
- Other problems – who gets first right to tax  
Answer - foreign country where trust is resident

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## Canadian Persons, U.S. Beneficiaries

U.S. Resident Trust	International Trust
Canadian tax unless income paid out. If income retained, foreign tax credit given in Canada for U.S. tax paid	Canadian tax unless income paid out
No UNI problem	If income retained, tax deferral but UNI problem at future date
Deemed gain every 21 years, and on death of Canadian contributor	Deemed gain every 21 years, and on death of Canadian contributor
No need to pay out income to manage Canadian and U.S. tax position	Need to pay out income Each year to prevent UNI

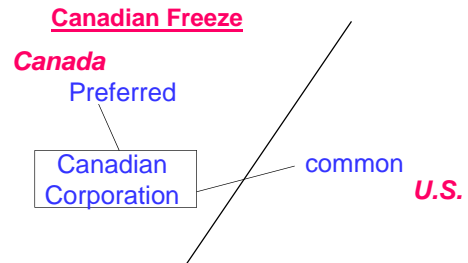
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## Canadian Persons, U.S. Beneficiaries

- Evaluation of U.S. v. international trust is U.S. tax issue
- Trust is valuable for U.S. estate tax sheltering/may be tax neutral for income tax

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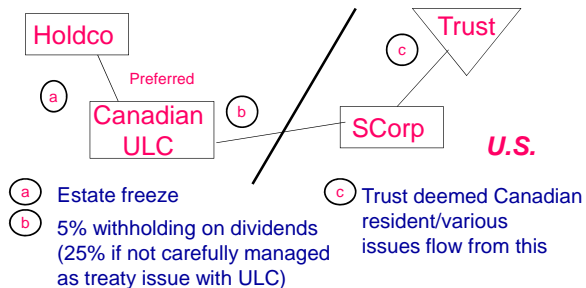
## Canadian Persons, U.S. Beneficiaries



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## Canadian Persons, U.S. Beneficiaries

### Canadian Freeze/U.S. Version



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## Canadians with U.S. Assets

- Canadians often own U.S. assets
- U.S. estate tax issues
- How best to hold the assets (especially U.S. real estate)

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## Canadians with U.S. Assets

Canadian capital gains tax	23%
U.S. estate tax	40%

Capital gain based on gain  
Estate tax based on value,  
but exemption \$5.4 million (2014)  
(possible to double exemption with spouse  
and others)

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## Canadians with U.S. Assets

### U.S. Situs Assets

U.S. real estate (personal, rental, business)  
U.S. stocks (U.S. domestic corporation)  
U.S. LLCs or partnerships with U.S. assets  
U.S. stock options  
Certain U.S. debts (but unusual)

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## Canadians with U.S. Situs Assets

### Canada-U.S. Treaty

- \$5.4 million unified credit (2014)(pro rated)
- Additional marital credit (limited to pro rated unified credit)
- Credit in Canada for estate tax against Canadian capital gains tax (federal)

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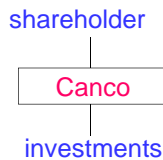
## Canadians with U.S. Assets

- Determine which assets are U.S. situs
- Determine U.S. estate tax exposure (note pro-rated exemption)
- Move certain assets to Canadian corporation
- Sell or gift other assets (caution for gift of U.S. real estate due to gift tax)
- Possible use of a trust
- Residual exposure, consider insurance and foreign tax credit in Canada for U.S. estate tax, or just live with it

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## Canadians with U.S. Assets

Normal for Canadians to use holding company



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## Canadians with U.S. Assets

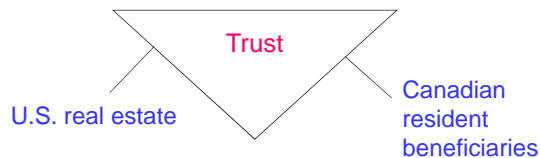
Portfolio investments move to Canadian holding company

### Problem Assets

- U.S. real estate
- U.S. LLCs (private business)
- U.S. securities in retirement plans
- U.S. stock options

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## Canadians with U.S. Assets

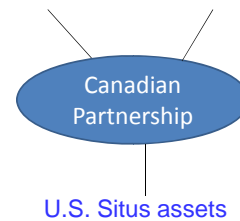


Use a trust to own U.S. real estate assets  
 Match foreign taxes  
 Long term capital gain treatment (individual)  
 No personal benefit (if personal use)

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## Canadians with U.S. Assets

Foreign Partnership Plan



Elect post death for partnership to be a corporation  
 75 days retroactive (to pre-death)

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## U.S. Persons with Canadian Assets

- After major changes in 2010, main area of exposure is limited to Canadian real estate and Canadian resource properties
- Capital gain taxable in Canada on sale, gift, death, 21 Yr rule if a trust
- Includes indirect holdings (even shares of foreign corporation)

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## U.S. Persons with Canadian Assets

Canadian rental income taxable at 25% withholding on gross rent or net election at regular rates

Clearance certificate process on sale or 25% withholding on sale proceeds (like FIRPTA)

Best structure for personal real estate likely U.S. LLC or S Corp.

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## Canadians Moving to U.S.

Leaving Canada	Arriving U.S.
Deemed sale of assets, capital gains	Step-up in basis (given by Treaty)
Future liability to tax for Canadian real estate holdings	U.S. estate and gift tax system
Canadian tax issues of structure ongoing	U.S. tax issues of structure ongoing

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## Canadians Moving to U.S.

### Departure Tax

- Capital gains tax
- Pay v. furnish security
- Structures to avoid or defer or reduce departure tax
- Needs advance planning
- Potential for double taxation

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## Canadians Moving to U.S.

### U.S. Basis of Assets

- Step-up in basis of assets held direct
- Various ways to arrange step-up for indirect holdings
- Use of ULCs (step-up corporate assets)
- Use of LLCs
- Use of foreign hybrid and check the box
- Transfer from one retirement plan (eg, RRSP) to another

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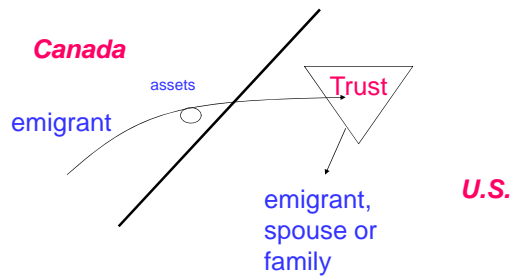
## Canadians Moving to U.S.

### U.S. Estate Tax

- Transfer assets to a trust (Canadian, U.S., foreign?)
- Best to do pre-arrival in U.S. (possibly shortly after but depends if hold green card or not)

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## Canadians Moving to U.S.



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## Canadians Moving to U.S.

U.S. or foreign trust may have ongoing liability to Canada if:

- Property transferred from Canadian resident or
- Property transferred from person now non-resident but Canadian resident in past 60 months and Canadian beneficiaries of trust (or ability to add) (Canadian resident who can only benefit after death of related person is excluded)

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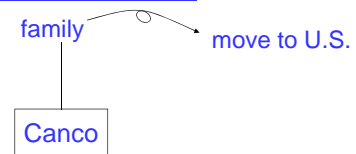
## Canadians Moving to U.S.

- Ongoing Canadian capital gains tax liability for Canadian real estate (or shareholdings where real estate is over 50% of value)
- Stock option benefits (employment)
- Retirement plans (withholding tax)

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## Canadian Persons Moving to U.S.

### Reducing Departure Tax



Reduce value of Canco by paying out dividends pre-departure  
Consider converting Canco to a ULC  
Double tax issues within Canco – withholding on dividend payment

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## U.S. Persons Moving to Canada

- U.S. family moving to Canada
- Various assets, sources of income
- U.S. citizen/long term green card holder/short term green card holder/other

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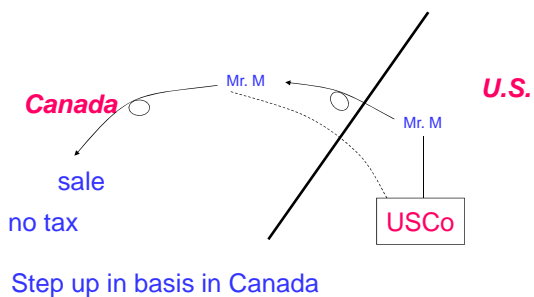
## U.S. Persons Moving to Canada

Arriving in Canada	Leaving U.S.
Step-up in basis except Canadian real estate holdings	No departure tax unless expatriation U.S. citizen or green card holder still taxed
Foreign trust taxable from January 1	Otherwise no ongoing capital gains tax except for U.S. real property and U.S. business assets
	But beware special rules on grantor trusts

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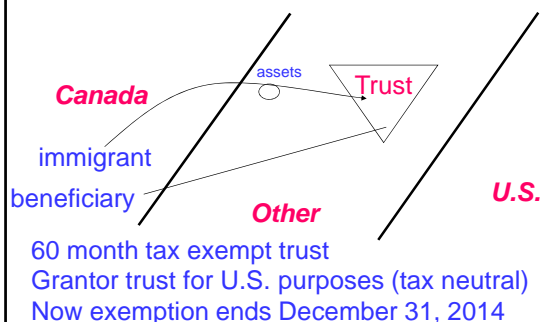


## U.S. Persons Moving to Canada



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## U.S. Persons Moving to Canada



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## U.S. Citizens Living in Canada

- U.S. citizen and family living in Canada
- Wishes to do estate planning
- What structures are available?

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## U.S. Citizens Living in Canada

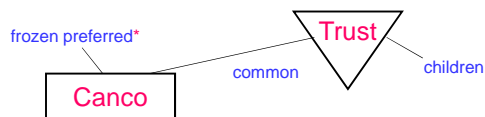
- Many do not comply, no U.S. filings
- What happens on death?
- Canadian income tax/U.S. estate tax
- Often spouse is NRA
- Catch-up filings?
- Expatriation?
- Are children U.S. citizens?

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## U.S. Citizens Living in Canada

### Canadian Estate Planning

Estate freeze for capital gains purposes,  
pass growth to children



\*non-cumulative dividends, usually not paid

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## U.S. Citizens Living in Canada

### Canadian Estate Planning

- Use of insurance, often corporate-owned
- Use of corporation for investment assets
- No need to gift or deal with unappreciated property (no tax on death)

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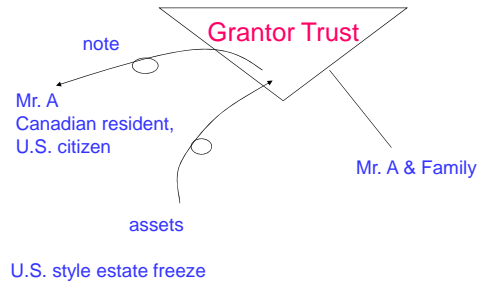
## U.S. Citizens Living in Canada

### U.S. Estate Planning Concepts

- Own investment assets personally
- Gifting program with limits
- Use of insurance non-corporate form, beneficiary the estate
- Use insurance trust
- Estate freeze, corporate v. intentionally defective grantor trust
- U.S. estate tax is dominant issue

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## U.S. Citizens Living in Canada



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## U.S. Citizens Living in Canada

Canada	U.S.
Trust reversionary	Trust reversionary
Income and gains taxed to Mr. A	Income and gains taxed to Mr. A
Capital gains tax on transfer to trust (but exceptions)	No tax on transfer to trust
No tax on Mr. A's death (but exceptions)	Estate tax on Mr. A's death on value of note
Taxable rollout from the trust to children	
Deemed capital gains every 21 years	

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## U.S. Citizens Living in Canada

- Canadian estate planning and U.S. estate planning are different
- Need to carefully coordinate all aspects to avoid a disaster and monitor regularly

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## Canada-U.S. Estate Planning

### Conclusions

- Very complex
- Big benefits from planning long term
- Huge traps
- Plan early/Plan often
- Get expert advice in both countries

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