

ESTATE PLANNING FOR DUAL CITIZENS

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DISCLAIMER

The information presented in this presentation is not intended to be legal advice and cannot be relied upon. The issues are presented in a summary fashion. Many of the conclusions presented are the opinions of the presenter based on individual research and analysis and may differ from the opinions of other tax professionals. Webinar participants should seek tax advice specific to their own situations as the law discussed here is quite complicated and the penalties involved can be quite steep.

ABOUT MAX REED



Max can be reached at:

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Max solves US tax problems for Canadians including:

- Adding corporations on the UX tax implications of cross-border transactions and initial public offerings;
- Helping citizens in Canada deal with US tax issues including renouncing their US citizenship; and
- Advising Canadian investment funds on investments into the United States and receiving investments from US taxpayers.

Max is the co-author (with Dick Pound of Stikeman Elliot) of A Tax Guide for American Citizens in Canada, as well as over 20 technical and plain language articles on a wide range of cross-border tax topics. Recognized for his expertise, Max is often invited to speak at conferences and seminars for tax professionals and the general public. He was invited to testify before the Canadian House of Commons Finance Committee on the impact of US tax law on Canadians.

Prior to joining SKL, Max worked at White & Case LLP, an international law firm in new York City where he provided US tax advice to individuals, corporations, and foreign states.

He holds a BA and two law degrees from McGill University, where he won several academic and leadership awards and is admitted to the bars of BC and New York.

WHO WE ARE

- Our new firm name!
- Canada/US cross-border tax law firm
- Lawyers in Toronto and Vancouver
- We do:
 - Cross-Border Estate Planning/Inheritance
 - Cross-Border Corporate Tax planning
 - Tax and immigration services related to renunciation
 - Help with your client's tough issues
 - Disputes with IRS (including penalty resolution and voluntary disclosures)
- We don't do: compliance work

TODAY'S AGENDA

1. Part 1 – Estate planning basics
2. Part 2 – Tax basics
3. Part 3 – Basics of wills and probate
4. Part 4 – Advanced Topics
5. Questions

PART ONE

BASICS OF ESTATE PLANNING

WHAT IS ESTATE PLANNING?

- Planning how your assets are distributed on your death in order to:
- Ensure that family members are taken care of
- Give to charity
- Achieve other objectives

ESTATE PLANNING 101

- A will – a legal document that directs where your assets go at your death
- Probate – the formal proving of the validity of a will
- Probate fees – tax on property passing through declared, probated estate
- Trust – a tool that can help you accomplish specific objectives after you pass away
 - Can be set up during your lifetime or at your death
- Beneficiaries – certain financial products, such as an RRSP, can have the beneficiaries designated without issue

HOW TO PLAN YOUR ESTATE

- It depends on complexity
- *Do-it-yourself*: There are kits and forms available
 - Often source of problematic and expensive estate settlement
- *Formal*: expertly drafted, trusted by banks, etc
- Paralegals/notary public in some provinces can draft simple documents
- More complex scenarios should get some legal/tax advice – there are a lot of tricks and traps

PART TWO

TAXES AT DEATH

TAX OVERVIEW

- Both countries impose tax on deceased, not on the person receiving the gift
 - Some US states have inheritance tax
- Beneficiaries inherit property at its fair market value at the time that the person dies
- Generally, no tax due until second of both spouses dies
- Canada has a capital gains tax at death
- US has an estate/gift tax

CANADIAN INCOME TAX AT DEATH

- Canada has a capital gains tax at death
- E.G. - you buy a share of Apple for \$5 and at the time you die it is worth \$15 = \$10 of capital gains
- Principal residence (i.e. your house) is exempted
- Spousal rollover – no tax due on first spouse to die

US FEDERAL ESTATE TAX

- All US citizens subject to estate/gift tax
- \$ 11.4 million lifetime exemption per US citizen
- Threshold will be reduced in 2025
- No US capital gains tax at death (yet)
- Credits available for Canadian tax
- Estate tax exemption might be reduced; now is a good time to plan

STATE ESTATE TAX

Following states have their own estate tax:

- Connecticut
- Hawaii
- Illinois
- Maine
- Maryland
- Massachusetts
- Minnesota
- New York
- Oregon
- Rhode Island
- Vermont
- Washington

US FEDERAL ESTATE TAX (2)

- Gifts subject to gift tax reduce estate tax exemption
 - I.e. Make gift of USD \$114,000 to child -> estate tax exemption reduced by USD \$100,000
 - Now USD \$11.3 million
- Gifts > USD \$14,000: reduces estate tax exemption
 - Form 709
- Gifts to non-US spouse > USD \$ 155,000: reduces estate tax exemption
 - Form 709

RRSPs/RRIFs

- During lifetime, tax deferred in both Canada/US under Canada-US Tax Treaty
- Canada – at death can transfer tax deferred to spouse or disabled child
- Taxable when second spouse dies
- US – at death can be rolled over to a spouse. US taxation at death is complicated
- Designate beneficiaries of RRSPs to avoid probate

CHARITABLE GIVING

- Bequests to charity can reduce capital gains and estate tax at death
- Gifts to both Canadian and US charities can reduce US federal estate tax
- Gifts to US colleges/universities that the donor or donor's family attended are fully creditable against Canadian capital gains tax
- Canadian tax benefit for gifts to other US charities is limited to 75% of US source income
- Best strategy is to give to Canadian charities

SALE OF PRINCIPAL RESIDENCE

- Canada – sale of principal residence tax free
- US – only \$250,000 (\$500K if married to an American) of gain tax free
- Many US citizens in Canada may have US capital gains exposure on their homes
- More info → <https://skltax.com/real-estate-ownership-u-s-citizens-canada/>

SALE OF PRINCIPAL RESIDENCE

- Transfer ownership of home to non-US spouse
 - Either all at once or in tranches
 - No Canadian tax on the transfer
 - Likely no real property transfer taxes
 - Possibly a gift in US (depending on value of transfer)
- Bequeath the home to your children
 - No Canadian tax
 - Avoids US capital gains tax because there is no sale
 - Probate fees

SALE OF HOME - EXAMPLE

- Couple bought house in 1998 for CAD \$200,000
- They own it 50/50
- House is now worth CAD \$1.5 million (CAD 650K/gain each)
- Only one spouse is a dual citizen
- Transfer ownership from dual citizen spouse to non-dual citizen spouse so that no US capital gains due on sale
- Transfer should be tax free, but may require reporting
- Get some advice on the transfer

CANADIAN ESTATES = CANADIAN EXECUTOR

- One common trap is for Canadians to have a sole non-Canadian resident executor
- This can cause tax problems with the estate
- US based executor may have problems with Canadian estate
- Better to have estate managed from Canada – even if executors are joint
- See → <https://skltax.com/tax-issues-when-canadians-have-u-s-executors/>

PART THREE

BASICS OF ESTATE LAW

INTRO TO ESTATE LAW

- Each province/state has own rules
- Will is basic estate planning document
- If no will → intestacy → default rules set by government
- Wills are probated by a court
- Probate fees can be expensive – up to 1.5% of amounts over \$50,000
- Avoidable through the use of a trust

POWER OF ATTORNEY

- A legal document that allows someone else to make decisions on your behalf if you are unable to speak for yourself (incapacitated or extended absences)
- Power of attorney over property – allows decision making over property (i.e. paying bills, maintaining investments)
- Power of attorney for personal care – allows decision making for health care
- Each province has different rules

ASSETS IN MULTIPLE PLACES

- Each state/province has its own rules on whether a will is valid See → <https://skltax.com/estate-planning-for-canadians-with-us-real-estate/>
- A will in one country may not work in the other country
- Scenario
 - James lives in Ontario but has a Florida condo
 - His Ontario will leaves condo to son, not spouse
 - Ontario will may not work in Florida
 - Florida default laws may require condo to go to spouse
- Solution:
 - A will in each jurisdiction you have assets
 - International will
 - Use a trust

PART FOUR

COMMON ISSUES - ADVANCED TOPICS

WHEN TO GET PROFESSIONAL HELP

- You are setting up a trust or receiving money from it
- You are inheriting money from your US parents
- You own a US LLC and live in Canada
- You provide services through a Canadian corporation
- You are planning your estate and it has property in both countries
- You want to renounce your citizenship
- You have a 401K in the US – may be good time to repatriate money to Canada

TRUSTS

- A trust is a legal relationship that survives your death
- Can be set up during your lifetime or as part of your will
- Can be used to put conditions on the transfer of assets after your death
 - I.e. Child gets 25% of assets at age 25; rest at age 40
- Trust rules are different in both countries
- Lots of potential for double tax
- **Always** get tax advice in both countries on trusts

US LLCs/LLPs/LLLPs

- US lawyers often advise Canadians to buy real estate through LLCs/LLPs/LLLPs
- LLCs/LLPs/LLLPs are flow through in US but corporations in Canada
- High potential for double taxation – 62% tax rate
- Solution:
 - Don't invest in US through LLCs
 - If have an LLC → **get tax advice ASAP**

INHERITANCE FROM US PARENTS

- Generally no inheritance tax in either country
- Both countries give you an increase in cost basis when you inherit assets through a will
- Cost basis = purchase price
- EG:
 - Mom bought a cottage for US\$100,000
 - The cottage is now worth US\$250,000
 - Mom dies and you inherit the cottage
 - Your cost basis in the cottage is US\$250,000
 - Sell for US \$260,000 – US \$10,000 of capital gain in both countries

INHERITANCE FROM US PARENTS

- Many US residents use a trust to avoid probate
- Assets in these trusts will have an increased cost basis in the US because the US ignores the trust
- Canada does not give you an increase in basis
 - Mom bought a cottage for US\$100,000
 - Put it in a trust in the US
 - Mom dies and the cottage is worth US \$250,000
 - Months later, trustee sells the cottage for US \$260,000
 - US \$10,000 in taxable capital gain
 - But in Canada US \$160,000 in taxable capital gain

INHERITANCE FROM US PARENTS

- Don't use probate avoiding trusts in the US
- Get some Canadian tax advice before distributions are made
- Sell assets in one year and distribute them in the next year
- Make the trust establish Canadian tax residency

FURTHER READING

- Renouncing US citizenship → <http://www.skltax.com/renouncing-us-citizenship-after-us-tax-reform/>
- Inheriting money from the US → <https://skltax.com/the-tax-consequences-of-inheriting-money-from-the-u-s/>
- US citizens in Canada owning US real estate -> <https://skltax.com/real-estate-ownership-u-s-citizens-canada/>

FURTHER READING

- Tax issues when Canadians have US executors → <https://skltax.com/tax-issues-when-canadians-have-u-s-executors/>
- 3520/A penalties → <https://skltax.com/watch-out-for-form-3520-and-form-3520-a-penalties/>
- Estate planning for Canadians with US real estate → <https://skltax.com/estate-planning-for-canadians-with-us-real-estate/>

QUESTIONS?

THANK YOU!