



STEP LONDON & SOUTHWESTERN ONTARIO CHAPTER LAUNCH EVENT

THURSDAY, October 17, 2013 @ 4:30 p.m.

U.S. TAX UPDATE: ISSUES THAT CANADIAN ADVISORS SHOULD BE AWARE OF FOR THEIR CLIENTS

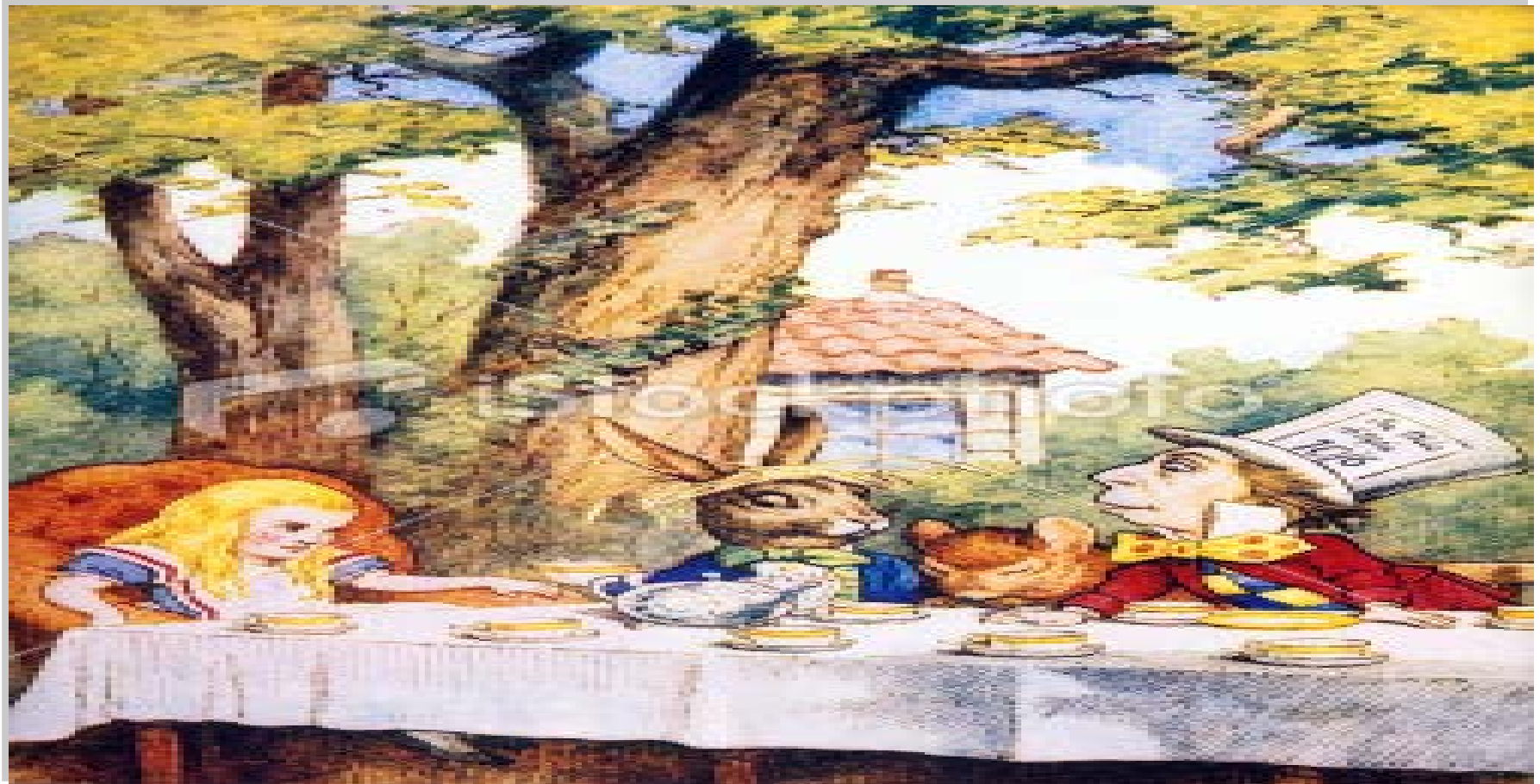
Speaker : Edward Northwood, The Ruchelman Law Firm, Toronto

Topics

- 1. Current status of US legislative changes as affecting cross border estate planning and FATCA (Foreign Account Tax Compliance Act) phase-in**
- 2. Summary of implications of US citizens and green card holders giving up US status**
- 3. Brief review of options for acquiring and holding US real property.**



THE GIFT AND ESTATE TAX SURPRISES



PRIMARY INDIVIDUAL INCOME TAX CHANGES

- Top federal rate now 39.6% on ordinary income over \$400K (\$450K joint) for US taxpayers
- Long term capital gains and qualifying dividends tax rate now increased to 20% for same classes of taxpayers (which will apply to Canadians who sell US real properties)
- Itemized deductions and personal exemptions phased out or limited for those with income over \$250K (\$300K joint)
- NB – 3.8% additional tax on net investment income for US taxpayers with income over \$200K (\$300K Joint) now in effect (under “Obamacare” law); this does not apply to NRAs



GIFT AND ESTATE TAX CHANGES EFFECTIVE FOR 2013 UNTIL.....

- US Gift, Estate and GST Tax Exemption all = \$5M, Indexed for Inflation
[2012 = \$5.12M; 2013 \$5.25M]
- Tax Rate for transfers over \$1M = 40%
- Portability for U.S. spouses
 - Essentially, unused exemption on first death may be used on second death
- All permanent (that is, no “sunset”)
- Many States still impose a separate estate tax

WHAT DID NOT CHANGE

- Valuation discounts for Family LP's and Companies remain
- QDOT Laws still apply
- Canada/US Treaty applies to Increased Estate Tax Exemption and Death Tax Credits
- DOD Basis Bump remains applicable to all Decedents' Assets [both US citizens, US domiciliaries and NRA's]
- State estate taxes remain a deduction for federal purposes (there used to be a credit)

CANADA/U.S. TREATY – DEATH TAXES

- Prorated unified credit
 - [US situs assets/worldwide estate] x U.S. credit
 - Means that if net worth < \$5M, no U.S. estate tax on U.S. assets
- Marital credit = additional [prorated] unified credit
- Canadian capital gains and accrued income taxes creditable as foreign death tax (and vice versa)
- **TREATY ELECTION REQUIRED**

U.S. CONGRESS' AND IRS' OBSESSION WITH FOREIGN REPORTING

- Offshore Voluntary Compliance
 - 2009 OVC Program
 - 2011 OVD Initiative
 - 2012 Continuation of OVDI, but meaner
 - “Relief” for Canadian residents
 - IRS Fact Sheet 2011-13
 - Streamlined Filing Guidance published 31st August 2012
- FATCA “whistle-blowing” (effective 2014)

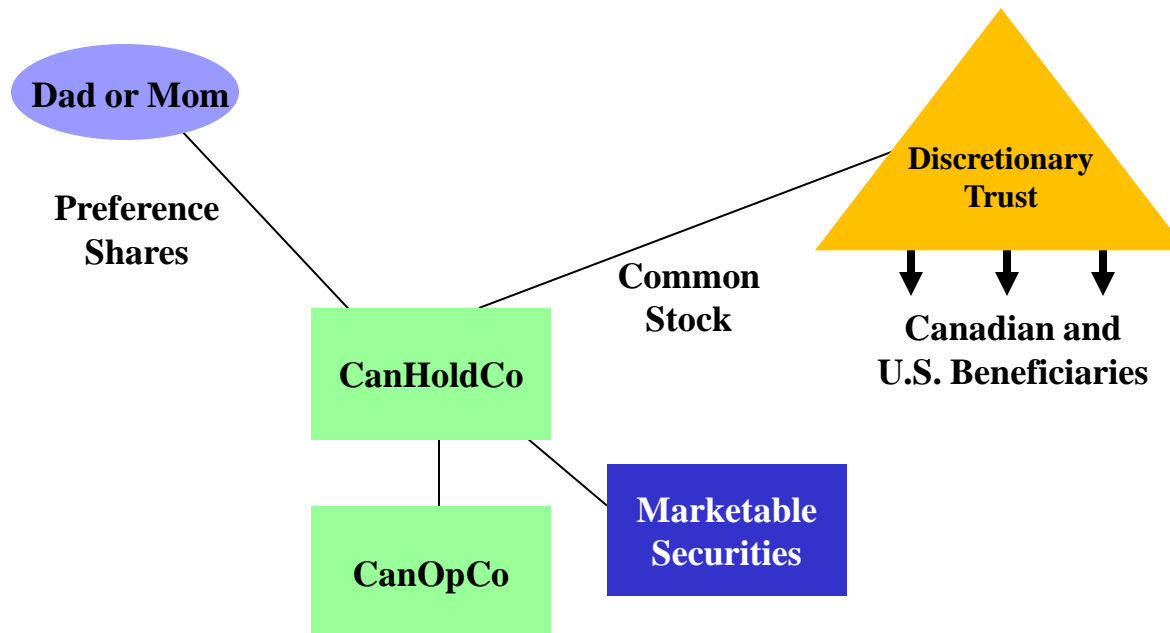
POT POURRI OF FOREIGN COMPLIANCE FORMS

- FBAR (TD F 90-22.1)
- 8938 (attachment to 1040)
- 5471 (CFC)
- 8621 (PFIC)
- 8891 (RRSPs)
- 3520 and 3520-A (Foreign Trusts)
- Failure to timely file any of these can lead to substantial penalties, even if no income tax owed!



COMMON CANADIAN STRUCTURES EXPOSING U.S. TAXPAYERS TO ANTI-DEFERRAL RULES

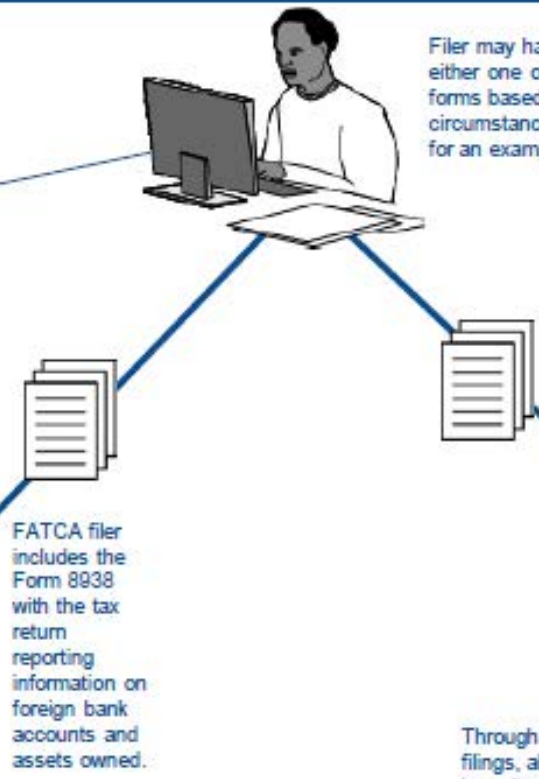
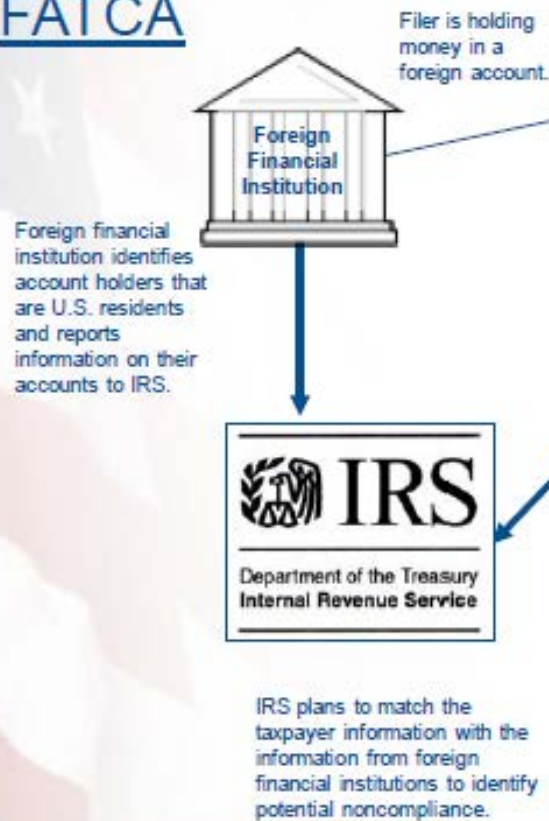
Typical Canadian Freeze



Background

Figure 1: Illustration of Information Reporting under FATCA and FBAR

FATCA



Filer may have to report on either one or both of the forms based on their specific circumstances. See table 2 for an example.

FBAR



Figure 2: Duplicative or Similar Reporting Requirements



GAO

Accountability • Integrity • Reliability

Form 8938 November 2011 Department of the Treasury Internal Revenue Service	Statement of Specified Foreign Financial Assets ▶ See separate instructions ▶ Attach to your tax return	CMS No. 1540-2165 Attachment Sequence No. 475
If you have attached additional sheets, check here <input type="checkbox"/>		
Name(s) shown on return		Identifying number
Number, street, and room or suite no. (if a P.O. box, see instructions)		
City or town, province or state, and country (including postal code)		
For tax year beginning 20... and ending 20...		
Note: All information must be in English. Show all amounts in U.S. dollars. Show currency conversion rates in Part I, line (6), or Part II, line (6).		
Type of filer a. Specified individual (1) <input type="checkbox"/> Married filing a joint return (2) <input type="checkbox"/> Other individual b. Specified domestic entity (1) <input type="checkbox"/> Partnership (2) <input type="checkbox"/> Corporation (3) <input type="checkbox"/> Trust (4) <input type="checkbox"/> Estate		
Check this box if this is an original, amended, or supplemental Form 8938 for attachment to a previously filed return		
Part I. Foreign Deposit and Custodial Accounts (see instructions)		
If you have more than one account to report, attach a continuation sheet with the same information for each additional account (see instructions).		
1. Type of account <input type="checkbox"/> Deposit <input type="checkbox"/> Custodial	2. Account number or other designation	
3. Check all that apply: a. <input type="checkbox"/> Account opened during tax year b. <input type="checkbox"/> Account closed during tax year c. <input type="checkbox"/> Account jointly owned with spouse d. <input type="checkbox"/> No tax has been reported in Part II with respect to this asset		
4. Maximum value of account during tax year \$		
5. Did you use a foreign currency exchange rate to convert the value of the account into U.S. dollars? <input type="checkbox"/> yes <input type="checkbox"/> no		
6. If you answered "yes" in line 5, complete all that apply:		
(1) Foreign currency in which account is maintained	(2) Foreign currency exchange rate used to convert to U.S. dollars	(3) Source of exchange rate used if not from U.S. Treasury Financial Management Service
7. Name of financial institution in which account is maintained		
8. Mailing address of financial institution in which account is maintained: number, street, and room or suite no.		
9. City or town, province or state, and country (including postal code)		

TD F 90-22.1 Rev. January 2011 Department of the Treasury Do not use previous editions of this form	REPORT OF FOREIGN BANK AND FINANCIAL ACCOUNTS Do NOT file with your Federal Tax Returns	OMB No. 1545-0048 This Report is for Calendar Year Ended 2011 Account type <input type="checkbox"/>
Part I. Filer Information		
1. Type of filer: <input type="checkbox"/> Individual <input type="checkbox"/> Partnership <input type="checkbox"/> Corporation <input type="checkbox"/> Consistent <input type="checkbox"/> Foreign in Other—Enter type		
2. U.S. Taxpayer Identification Number	3. Foreign identification (Complete only if item 2 is not applicable) a. Type: <input type="checkbox"/> Passport <input type="checkbox"/> Other	4. Individual's Date of Birth (MM/DD/YYYY)
5. Last Name or Organization Name	6. First Name	7. Middle Initial
8. Address (Number, Street, and Apt. or Suite No.)		
9. City	10. State	11. Zip/Postal Code
12. Country		
13. Does the filer have a financial interest in 20... or more financial account(s)? <input type="checkbox"/> Yes. If "Yes" enter total number of accounts: _____ (If "Yes" is checked, do not complete Part II or Part III, but enter details at this information) <input type="checkbox"/> No		
Part II. Information on Financial Account(s) Owned Separately		
14. Maximum value of account during calendar year reported	15. Type of account: <input type="checkbox"/> Bank <input type="checkbox"/> Securities <input type="checkbox"/> Other—Enter type below	
16. Name of financial institution in which account is held		
17. Account name or other designation		
18. Mailing address (Number, Street, Suite Number) of financial institution in which account is held		
19. City	20. State	21. Zip/Postal Code
22. Country		

Duplicate identifying information Similar reporting requirements Duplicate account information

Source: GAO analysis of the Form 8938 and FBAR.



Supplement 1

Table 3: Comparison of Form 8938 and FATCA Penalty Regimes

	Form 8938	FBAR
Failure to File	\$10,000	Maximum of \$10,000
Continuing Failure to File	After 90 days from notice, an additional \$10,000 for each 30 day period. Maximum additional penalty is \$50,000	not applicable
Reasonable cause exception	Yes	Yes
Accuracy-related penalty	40 percent of the underpaid tax amount	not applicable.
Willful failure to file or willfully causing another to fail to file	not applicable	\$100,000 or 50% of the account balance, whichever is greater
Fraud	75 percent of the underpaid tax amount attributable to fraud	not applicable
Criminal Penalties	Yes	Yes
Statute of Limitations	3 years after the date of filing or from when the information is reported to IRS and 6 years after the return was filed if the taxpayer fails to report over \$5,000 in gross income from foreign assets	6 years to assess penalty and 2 additional years to collect after assessment



LEAVING AMERICA (AND STOPPING TAXATION)

- If U.S. citizen, or Long Term Permanent Resident, Expatriation rules apply
- All others, fail the days' test (and really depart)
 - Beware retained US situs assets subject to US estate tax
 - Plan for continuing US source income

NEW EXPATRIATION LAW

- Applies to US Citizens and Long Term Permanent Residents expatriating after 16 June 2008, repealing 2004 law
- Exit Tax – similar to Canada but more mean-spirited
 - Deemed sale of all assets, with ability to defer (with interest); applies to Grantor Trust assets as well as personally owned
 - Tax on deemed sales only applies on total gain over \$600,000 (indexed for inflation)
 - LTRs use U.S. entry date fmv as cost basis



NEW EXPATRIATION LAW...CONTD...

- Immediate taxation of IRAs and RRSPs (and other tax deferred accounts, except for qualified retirement and pension plans)
- Non-Treaty withholding rates (30%) on deferred compensation plans (that are not tax deferred accounts)
- Nongrantor Trust: 30% withholding on distributions to covered expatriate (that would have been taxable income)



NEW EXPATRIATION LAW...CONTD...

- Applies to “covered expatriates” which is the same class as under 2004 law (more than \$2M net worth; or more than \$131,000 (indexed) average income tax liability for past five years; or cannot certify compliance with last five years of US tax return requirements)
- Important broader exception: dual citizen at birth; after expatriation will continue to be citizen and tax resident of Treaty country; failed the “days test” for 10 of previous 15 years; and has filed five most recent years of US returns.



NEW EXPATRIATION LAW ...CONTD...

- Tax on US recipients of gifts and inheritances from covered expatriates
 - Highest gift and estate tax rates
 - No exemptions (other than \$13,000 annual exclusion)
- Hassle visiting U.S.?



PLANNING FOR CANADIANS WITH U.S. SITUS PROPERTY



- Individually
- Foreign Corporation
- Foreign Partnership
- Trust



OWN INDIVIDUALLY

- U.S. situs asset for U.S. gift and estate tax purposes
- Treaty relief
 - Prorated use of unified credit
 - Marital credit
 - Neither credit may be used for lifetime gifts
- Foreign death tax credits

OWN INDIVIDUALLY ...CONTD...

- Joint Ownership
 - Not effective for estate tax purposes, but simplifies transfer at death
 - Unified credit available along with treaty benefits (like marital credit)
 - May be appropriate in smaller estates
 - Possible gift at time of purchase
 - No unified credit or treaty benefits
 - Split purchase alternative
 - Tenancy-in-common ownership is better



OWN INDIVIDUALLY ...CONTD...

- Nonrecourse Mortgage
 - A dollar for dollar deduction against value of real property includible in estate
 - Becoming easier to obtain
 - Must be bona fide (may not be respected if obtained from a family member)
 - May give rise to income tax issues on interest paid in tax home



FOREIGN CORPORATION (HOLDCO)

- Increased income taxes [corporate rates]
- Deemed income (shareholder benefit) in Canada
- IRS “look through” position for estate tax purposes [other than sham companies, a foreign corporation should readily provide insulation]
- CFC if owner becomes U.S. tax resident [or shares inherited by U.S. persons]

FOREIGN PARTNERSHIP

- “Look-through”
- Check the box after death?
- Enterprise for foreign purposes?

TRUST ALTERNATIVE

- Form trust for benefit of spouse and descendants, fund with cash, and have trust purchase U.S. real property
 - Should not be in settlor's estate as long as use only at spouse's consent and not as a trust beneficiary
 - May be less likely to be challenged if descendants use property frequently as well
 - If spouse dies, settlor must pay rent to use the property
 - Avoids deemed income issues
 - Must address special rules in jurisdiction applicable to trust's taxation



DISCLAIMER

NOTE TO READERS

- This Presentation is not intended to be legal advice
- Reading the materials does not create an attorney-client relationship
- The outcome of each case stands on its own merits
- Pursuant to I.R.S. regulations, any conclusions or comments contained herein is not intended or written to be used, and cannot be used by the reader, for the purpose of avoiding tax penalties