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Charles W. Cullen III, CIM, CFP
Tél. : 902-424-1092
charles.cullen@rbc.com

U.S. revocable living trusts for Canadian residents

Are they a problem in Canada?

Canadian residents, including those who are U.S. persons living in Canada (i.e. U.S. citizens and U.S. Green Card holders) may be exposed to various tax and estate planning problems stemming from differences in the tax and legal treatment of U.S. revocable living trusts in Canada versus in the U.S. This article examines some of the potential issues that may arise where a Canadian resident is the settlor, the sole trustee and the beneficiary of a U.S. revocable living trust. This article also discusses some of the issues a Canadian resident may experience as a residual beneficiary of a U.S. revocable living trust. If your U.S. revocable living trust structure is different, this article may not apply to you.

Overview of U.S. revocable living trusts

A U.S. revocable living trust (also referred to as a grantor trust in the U.S.) is commonly used in the U.S. for estate planning, primarily for probate minimization and incapacity planning. It generally does not provide creditor protection to the grantor. Most of these trusts are drafted to permit you to revoke or amend them whenever you wish to do so. The parties to a U.S. revocable living trust include a settlor (also referred to as a grantor), a trustee, a beneficiary and a residual beneficiary or beneficiaries.

The grantor settles the U.S. revocable living trust by transferring property to the trustee, and the trust document deals with the distribution of the property upon the death of the grantor. Often, a clause is added in the grantor's Will referred to as a "pour-over" clause. This clause provides for property in your estate that had not already been transferred to your U.S. revocable living trust during your lifetime to be transferred to the trust upon your death. This allows for the property in your estate to also be dealt with according to the provisions set out in the revocable living trust agreement.

A typical structure for a U.S. revocable living trust is where the grantor, trustee and beneficiary are the same individual. This article focuses on this typical structure (except where specifically mentioned in the section, "Canadian resident residual beneficiary"). As a tool for incapacity planning, a successor trustee may be named. Should incapacity occur, the successor trustee takes immediate control of the property to use it for your care and support, or in whatever way you've directed by the terms of the trust.

While the grantor is alive, the grantor has access to both the income and capital of the trust. Residual beneficiaries named in the trust document cannot generally access the income or capital of the trust while the grantor is alive, but they will benefit from the trust property upon the grantor's death, at which point the trust generally becomes an irrevocable trust.

A U.S. revocable living trust may be created as a joint revocable living trust for spouses. After the death of the first spouse, the trust may continue as a revocable living trust during the lifetime of the surviving spouse. However, it is possible to transfer a portion of the trust property to irrevocable trusts for your spouse and other beneficiaries. For U.S. income tax purposes, you must be legally married to be considered spouses. Common-law couples are generally not considered spouses. Therefore, reference to spouses in this article for U.S. tax purposes refers to a legally married couple.

U.S. tax treatment

The U.S. disregards the existence of the revocable living trust for income tax purposes. This is due to the control of the trust property being maintained by the grantor and the grantor having reversionary rights. Income or capital gains earned on trust property is attributed to and taxable in the hands of the grantor during his or her lifetime. Since the grantor is normally the income beneficiary, this generally doesn't pose a problem for U.S. income tax purposes. Property with accrued gains may be transferred by the grantor to a U.S. revocable living trust and from the trust to the grantor without triggering U.S. income tax or U.S. gift tax.

Keep in mind, if you're a grantor who is a U.S. person, you're subject to U.S. income tax on your worldwide income, so all of the income you earn in the U.S. revocable living trust is included on your U.S. income tax return. If you're a Canadian resident but not a U.S. person, you're subject to U.S. income tax only on U.S source income earned in the trust. U.S. source income typically includes income and gains from U.S. real property (e.g. rental income and capital gains on the sale of U.S. real estate), income from a U.S. trade or business and dividends on shares of a U.S. company but not capital gains on the sale of shares of a U.S. company.

A U.S. revocable living trust may be created as a joint revocable living trust for spouses. After the death of the first spouse, the trust may continue as a revocable living trust during the lifetime of the surviving spouse.

A U.S. revocable living trust does not shield the grantor from U.S. estate tax. Therefore, as a grantor of the trust, you must continue to monitor and manage your U.S. estate tax exposure. Generally, U.S. estate tax exposure does not apply to residual beneficiaries of the trust until after the grantor's death; however, it is possible for the grantor to structure the U.S. revocable living trust to provide residual beneficiaries with U.S. estate tax protection.

Canadian tax treatment

The estate planning benefits discussed earlier, such as probate minimization and incapacity planning, may also apply in Canada; however, for Canadian income tax purposes, a U.S. revocable living trust may be treated differently than in the U.S. It is the Canada Revenue Agency's (CRA) opinion that U.S. revocable living trusts are not bare trusts. Therefore, they're generally not treated as a disregarded entity for Canadian income tax purposes and are considered to be a separate taxpayer. The key distinguishing factor between revocable living trusts and bare trusts is that revocable living trusts generally include a remainder or residual beneficiary so that there's a change of beneficial ownership when property is transferred to the trust. For the purposes of this article, a U.S. revocable living trust is not a bare trust, a qualifying disposition trust, a self-benefit trust, an alter ego or joint partner trust and is not a disregarded entity for Canadian tax purposes.

Where a trust exists and is not disregarded, it will be considered a Canadian resident trust if the central management and control over the trust property is conducted in Canada. A U.S. revocable living trust that's managed and controlled by a Canadian resident is resident in Canada for tax purposes. In general, where a trust is considered to be a Canadian resident trust, it would be taxable in Canada on its worldwide income. Even if the trust is managed and controlled outside of Canada, the trust is a deemed Canadian resident if a resident of Canada contributed to the trust. Note that this article does not address deemed residency since it focuses on U.S. revocable living trusts where the Canadian resident is the settlor, the sole trustee and beneficiary. The tax rules

related to deemed Canadian resident trusts are complex and are out of the scope of this article.

Where a person who's contributed property to the trust maintains control over the trust property, or where the property can revert back to them, and the trust is resident in Canada, subsection 75(2) of the Income Tax Act may apply. This subsection results in any income or loss from the property and any taxable capital gain or allowable capital loss from the disposition of the property to attribute to the contributor while they are alive and resident in Canada. Therefore, subsection 75(2) will apply to a typical U.S. revocable living trust, where the settlor/grantor, who is also the sole trustee, is resident in Canada.

Potential tax and estate planning issues for Canadian residents

A Canadian resident may be connected to a U.S. revocable living trust in a number of ways. You may have purchased U.S. real property through a U.S. revocable living trust or transferred U.S. real property or other U.S. property you own to the trust. Maybe you moved to Canada with a U.S. revocable living trust that you'd set up for yourself before you relocated to Canada. Or, you may be a residual beneficiary of a U.S. revocable living trust that was set up by another family member.

The following sections highlight various situations and some of the potential tax and estate planning issues involving a U.S. revocable living trust that may arise for Canadian residents.

Transferring property to a U.S. revocable living trust

For Canadian income tax purposes, a Canadian resident who transfers property to a U.S. revocable living trust is normally considered to have disposed of the property at its fair market value (FMV). As a Canadian resident grantor, you are subject to Canadian tax on the property's unrealized gains upon its transfer to the trust. On the other hand, for U.S. income tax purposes, there's no corresponding U.S. income tax triggered when property is transferred to the trust. The result is the possibility of double taxation, since the timing of Canadian and U.S. taxation may occur in different tax years, limiting the ability to claim a full foreign tax credit.

Let's look at an example. For simplicity, this example ignores differences in currencies and fluctuations in exchange rates. Assume you purchased U.S. real estate for $100,000, transferred it that same year to a U.S. revocable living trust when its FMV is $150,000, and three years later sold it for $200,000. On the transfer of the property to the trust, there is no U.S. income tax. As a Canadian resident, you're deemed to have disposed of the property at its FMV of $150,000, resulting in a $50,000 capital gain which is taxable in that year. There are no U.S. taxes paid to be able to claim a foreign tax credit against the Canadian tax. Then, three years later when the U.S. real estate is sold, you will have a gain for U.S. income tax purposes of $100,000 ($200,000 – $100,000). However, for Canadian tax purposes, your gain will only be $50,000 ($200,000 – $150,000). The foreign tax credit that may be claimed on your Canadian return will be limited to the Canadian income tax liability in the year of sale. To summarize, you paid tax in the U.S. on a gain of $100,000 and you paid tax in Canada on the same gain of $100,000, with a foreign tax credit claimed against only $50,000 of the gain. You were double taxed on a gain of $50,000.

> If you're the trustee of a U.S. revocable living trust and have become a Canadian resident, the trust also becomes a resident for Canadian tax purposes.

To minimize exposure to double taxation, it may be possible under the Canada-U.S. tax treaty to claim a deemed disposition of the property for U.S. income tax purposes at the time the property is transferred to the U.S. revocable living trust. In addition, you may prevent the double tax issue by funding a U.S. revocable living trust with cash to make the purchase of property instead.

Moving to Canada with a U.S. revocable living trust

If you're the sole trustee of a U.S. revocable living trust and have become a Canadian resident, the trust also becomes a resident for Canadian tax purposes. As a result, the trust is deemed to have disposed of and reacquired the trust property on the date it becomes resident in Canada. The adjusted cost base (ACB) of the trust property for Canadian tax purposes is the FMV of the property on this date. This means that accrued gains or losses on the trust property before this date are not applicable for Canadian tax purposes. Only further growth or decline in the value of the property is subject to Canadian taxation.

For U.S. income tax purposes, a move to Canada generally doesn't result in a disposition and there's no U.S. income tax triggered. Therefore, there's no change to the ACB of the property. In the future, when there is a disposition of the property, the gains and losses are calculated based on the original ACB of the property and subject to U.S. income tax at that time. For example, if the trust property was purchased for $100,000 and its value decreased to $90,000 at the time of moving to Canada, the ACB for Canadian tax purposes is $90,000, but it is $100,000 for U.S. tax purposes. If the property is sold for $100,000, there's a $10,000 capital

gain subject to Canadian tax, even though there's no gain in the U.S. The result is that the amount of the capital gain or capital loss subject to tax in Canada and in the U.S. may be significantly different.

Transferring property out of a U.S. revocable living trust

In many cases, the terms of a U.S. revocable living trust allow the grantor to instruct the trustee to transfer trust property as per the grantor's wishes to either the grantor or other family members, including persons who aren't current beneficiaries of the trust. In addition, trustee powers typically include the right to make discretionary distributions to the grantor and, sometimes, to the grantor's family, if the grantor becomes incapable.

If property is transferred out of a U.S. revocable living trust, there may be differing U.S. and Canadian tax implications and potentially double taxation. Double tax may arise due to differences in the ACB of the property for U.S. and Canadian tax purposes, mismatching in the timing of the taxation of income for Canadian versus U.S. tax purposes, the tax liability belonging to different taxpayers on each side of the border and the different types of tax that may apply.

Transfer to grantor

Generally, for Canadian income tax purposes, transfers of property from a U.S. revocable living trust to the grantor may occur on a tax-deferred rollover basis. This means the ACB of the property to the grantor will be equal to the ACB of the property to the trust immediately before the transfer out.

For U.S. tax purposes, a transfer of property from the trust to the grantor does not trigger U.S. income tax. The ACB of the property to the grantor will be equal to the ACB of the property to the trust immediately before the transfer out.

However, the ACB of the property to the trust for U.S. tax purposes could be different than for Canadian tax purposes. If the property is sold in the future, both Canadian and U.S. income tax will be triggered at the time of disposition; and although the amount of the gain for tax purposes could be different in the U.S. and Canada, foreign tax credits may be claimed to minimize double taxation.

Transfer to grantor's spouse from a joint U.S. revocable living trust

For Canadian tax purposes, generally, transfers of property from the trust to the grantor's spouse, as a beneficiary of the trust, may occur on a tax-deferred rollover basis. This means the ACB of the property to the spouse will be equal to the ACB of the property to the trust immediately before the transfer out.

For Canadian tax purposes, generally, transfers of property from the trust to the grantor's spouse, as a beneficiary of the trust, may occur on a tax-deferred rollover basis.

For U.S. tax purposes, a transfer of property from the trust to the grantor's spouse does not trigger U.S. income tax. However, U.S. gift tax may apply to the grantor if the spouse is not a U.S. citizen.[1] If the FMV of the property at the time of the gift exceeds the ACB of the property, the ACB of the property to the trust generally passes on to the spouse receiving the property. However, if the spouse is not a U.S. citizen and U.S. gift tax applies, the ACB of the property to the non-U.S. citizen spouse may be bumped up by a portion of the U.S. gift tax paid on the transfer. When the FMV of the property at the time of the gift is less than the ACB of the property to the trust, the ACB of the property to the recipient spouse is determined based on the value of the proceeds received when the property is eventually sold. A detailed discussion of the calculation of the ACB to the recipient spouse is beyond the scope of this article.

Whenever U.S. gift tax is incurred, there may be double tax. This is because foreign tax credits can't be claimed on a Canadian income tax return for U.S. gift tax. And, a deduction for Canadian income tax can't be claimed in the calculation of the U.S. gift tax liability. In addition, the ACB of the property to the recipient spouse for U.S. tax purposes could be different than for Canadian tax purposes. An eventual sale of the property by the spouse will trigger Canadian income tax on the gain to the grantor (if the grantor is still alive and resident in Canada) because of the attribution rules in Canada (a discussion of these rules is beyond the scope of this article). In the U.S., the sale will trigger U.S. income tax to the spouse. Because the income tax liability belongs to different taxpayers (grantor in Canada and spouse in the U.S.), foreign tax credits will not be available on a Canadian income tax return. Also, foreign tax credits may not be available in the U.S., except where the couple is filing a joint U.S. income tax return. As a result, there may be double taxation. Not only is the amount of the gain different in Canada and the U.S., but it's taxed in different individual's hands.

1) There are exemptions and credits that may result in no U.S. gift tax. The U.S. gift tax laws are not discussed in this article. For more information on U.S. gift tax, please ask your RBC advisor for the separate article on this topic and speak to a qualified U.S. tax advisor.

Other transfers

For Canadian tax purposes, transfers during the grantor's lifetime to someone who's not a current beneficiary of the trust, including the grantor's spouse, are at FMV and will trigger Canadian income tax to the grantor on the accrued gain in the year of the transfer. The ACB of the property to the transferee for Canadian tax purposes is the FMV at the time of the transfer. If the transferee is the grantor's spouse and the property has an accrued loss, the loss to the trust would be denied and be suspended in the trust until the property is actually sold to a non-affiliated person (a discussion of affiliated persons is beyond the scope of this article). The ACB to the spouse would still be equal to the FMV at the time of the transfer.

For U.S. tax purposes, a transfer of property from the trust does not trigger U.S. income tax. However, the transfer of property to anyone other than the grantor or the grantor's U.S. citizen spouse is considered a gift and may be subject to U.S. gift tax.[1] When U.S. gift tax is incurred, double taxation may result because U.S. gift tax and Canadian income tax do not offset each other. When the FMV of the gift exceeds the ACB of the property in the trust, the ACB of the property to the trust passes on to the individual receiving the gift. But, if U.S. gift tax is incurred on the transfer, as discussed earlier in the section describing transfers to a spouse, the ACB of the property to the recipient is bumped up by a portion of the gift tax paid. When the FMV does not exceed the ACB of the property in the trust, the ACB of the property to the recipient is determined based on the value of the proceeds received by the recipient when the property is sold.

The ACB of the property to the recipient may not be the same for Canadian and U.S. income tax purposes, whether or not U.S. gift tax is incurred. Therefore, there may be a significant difference in the amount of the gain on an eventual sale of the property. Also, there's the potential for double tax because a portion of the gain may have already been taxed for Canadian tax purposes in the grantor's hands at the time the property was transferred out of the trust. The double tax results because there's no ability to claim foreign tax credits, as different individuals are taxed and the tax may occur in different tax years. For example, let's assume there's a grantor who is a dual Canadian resident/U.S. citizen who funds the trust with $100,000 cash to purchase U.S. real estate. If the real estate is transferred to the grantor's adult child when the FMV is $150,000, it transfers at FMV triggering a $50,000 gain to the grantor for Canadian tax purposes. There is no U.S. income tax triggered on the transfer. However, the transfer results in a taxable gift in the U.S. The grantor may claim a U.S. gift tax exclusion and exemption so that there's no U.S. gift tax. As a result, the property transfers to the adult child at an ACB of $100,000 for U.S. tax purposes. If the adult child sells the property at $150,000, there's no gain triggered for Canadian tax purposes, but there would be a $50,000 gain for U.S. income tax purposes. The grantor has already paid Canadian tax on the $50,000 gain when the property was transferred out of the trust to the adult child. However, this $50,000 gain is taxable for U.S. income tax purposes to the adult child. So, it's being taxed twice, and there's no ability to claim foreign tax credits since the tax liability belongs to different people and in different tax years.

> For Canadian tax purposes, a Canadian resident trust (with the exception of certain types of trusts such as a self-benefit trust, an alter ego trust, joint spousal or common-law partner trust, post-1971 spousal or common-law partner trust) is generally subject to deemed disposition rules every 21 years, starting from the date the trust was created.

If trust property is transferred to the grantor's spouse and the property appreciates in value, an eventual sale of the property by the spouse will trigger Canadian income tax on the gain in the hands of the grantor (if the grantor is still alive and resident in Canada) because of the Canadian attribution rules. In the U.S., the sale will trigger U.S. income tax to the spouse. Because the income tax liability belongs to different taxpayers (grantor in Canada and spouse in the U.S.), foreign tax credits will not be available on the grantor's Canadian income tax return. Also, foreign tax credits may not be available in the U.S., except where the couple is filing a joint U.S. income tax return. As a result, there may be double taxation.

It may be possible to minimize or eliminate the double taxation. The grantor could make an election for U.S. income tax purposes at the time the property is transferred out of the trust, to treat the transfer as a disposition at FMV. As a result, the grantor would be subject to U.S. income tax and Canadian income tax at the time the property is transferred from the trust. This election would make sense where the U.S. income tax triggered on the accrued gain can be fully eliminated through claiming foreign tax credits ensuring no additional income tax burden to the grantor. In the earlier example, the result is that the ACB of the property to the adult child would be equal to the FMV of $150,000 for both Canadian and U.S. income tax purposes.

1) There are exemptions and credits that may result in no U.S. gift tax. The U.S. gift tax laws are not discussed in this article. For more information on U.S. gift tax, please ask your RBC advisor for the separate article on this topic and speak to a qualified U.S. tax advisor.

The tax election is for U.S. income tax purposes and has no bearing on whether U.S. gift tax is triggered when property is transferred from the trust. However, the grantor may use annual gift tax exclusions and gift tax exemptions where available.

21-year anniversary of a U.S. revocable living trust

For Canadian tax purposes, a Canadian resident trust (with the exception of certain types of trusts such as a self-benefit trust, an alter ego trust, joint spousal or common-law partner trust, post-1971 spousal or common-law partner trust) is generally subject to deemed disposition rules every 21 years, starting from the date the trust was created. The year in which a particular property was contributed to the trust or the year in which the trust becomes resident of Canada is not relevant for purposes of this rule.

When the 21-year deemed disposition rules apply, the trust is deemed to have disposed of and reacquired certain property at FMV, which triggers unrealized gains and losses even though the property has not actually been sold. When the U.S. revocable living trust is resident in Canada and subsection 75(2) applies, the capital gains and losses triggered by the 21-year deemed disposition rules will be attributed to the grantor.

For U.S. income tax purposes, the appreciation of property in a U.S. revocable living trust is generally not subject to taxation until the property is actually sold. As a result, there may be double tax when the 21-year deemed disposition rules apply. This is because the Canadian income tax is triggered in one year, while U.S. income tax is not triggered until the property is actually sold. It will not be possible to claim foreign tax credits where the taxation of the income in each country occurs in different tax years. However, it may be possible for the grantor to elect a deemed disposition for U.S. income tax purposes to mitigate double taxation. Double tax may also be prevented by transferring the property back to the grantor at the trust's ACB before the 21-year deemed disposition is triggered.

Leaving Canada with a U.S. revocable living trust

When you terminate your Canadian tax residency, you're deemed to have disposed of certain property for FMV on the date you become a non-resident. An exception applies for property you owned when you became a resident of Canada if, during the 10-year period immediately before ceasing to be a resident, you were not resident in Canada for periods totaling more than 60 months.

This exception does not apply to property in a trust or to a trust that ceases residency in Canada for tax purposes. Therefore, if the U.S. revocable living trust ceases to be resident in Canada, there will be a deemed disposition of the property in the trust for Canadian income tax purposes and, where subsection 75(2) applies, the grantor will be subject to Canadian tax on accrued gains.

> There's generally no Canadian income tax triggered for the trust when the grantor of a Canadian resident U.S. revocable living trust passes away.

Based on these tax implications, someone planning on moving to Canada on a short-term basis may benefit from winding up a U.S. revocable living trust before moving to Canada, which they may be able to do on a tax-free basis, and hold their property directly.

Taxation on death of a Canadian resident grantor

There's generally no Canadian income tax triggered for the trust when the grantor of a Canadian resident U.S. revocable living trust passes away. As a result, the ACB of the property for Canadian tax purposes does not change when the grantor passes away.

For U.S. estate tax purposes, the value of the property in a U.S. revocable living trust is generally included in the grantor's worldwide gross estate and the grantor may be subject to U.S. estate tax. The ACB of the property is bumped up to FMV on the date of death for U.S. income tax purposes, even if the grantor does not actually incur a U.S. estate tax liability. If the grantor is not a U.S. person, U.S. estate tax will only apply to property in the U.S. revocable living trust that is considered to have a U.S. location (U.S. situs property). If the grantor is a U.S. person for U.S. estate tax purposes, U.S. estate tax applies to all property in the U.S. revocable living trust.

Double tax may apply where a grantor is subject to U.S. estate tax upon their death on the value of the property in the trust. Canadian income tax on the accrued gain on the property is triggered in later tax years when the property is actually disposed of. For these reasons, U.S. revocable living trusts are generally not appropriate for Canadian residents who are exposed to U.S. estate tax.

Pour-over clause in a Will

The existence of a pour-over clause for U.S. estate planning purposes may work well in the U.S., allowing for property in your estate that had not been transferred to a U.S. revocable living trust during your lifetime to be transferred to it upon your death and dealt with according to the provisions set out by the revocable living trust. However, there's a significant estate planning risk for a Canadian resident who relies on such a clause in their Will. The risk is that Canadian courts generally consider

such clauses to be invalid. This may mean the property would not transfer to the U.S. revocable living trust and instead would become part of the residue of your estate and would need to be dealt with based on your Will. If your Will does not properly deal with this, the property may be subject to the intestacy laws. Therefore, if your Will contains a pour-over clause, consider amending or replacing it. Instead, you could create a testamentary trust through your Will that would have terms similar to the U.S. revocable living trust with respect to how to deal with property in your estate.

Transfer of property into a testamentary spousal trust

In Canada, on your death, you're deemed to have disposed of your property at FMV, except if the property is transferred to your spouse or to a testamentary spousal trust.[2] Such transfers occur at your ACB and result in a tax-deferred rollover. In addition, the 21-year deemed disposition rules discussed earlier do not apply to the testamentary spousal trust during your spouse's lifetime.

For U.S. planning purposes, your U.S. revocable living trust may provide for the property in the trust to transfer on your death to a U.S. estate tax protected spousal trust for the benefit of your surviving spouse. Unfortunately, this U.S. planning does not work effectively for Canadian residents. To benefit from the tax deferral on death and exemption from the 21-year deemed disposition rules in Canada, the U.S. estate tax protected spousal trust must be structured to also qualify as a testamentary spousal trust under Canadian tax law. To qualify as a testamentary spousal trust under Canadian tax rules, the trust must be created by provisions in your Will. In addition, the transfer of property to the trust must occur as a consequence of your death and not because of the terms of the U.S. revocable living trust.

For property already in a U.S. revocable living trust, while there may be no Canadian income tax on your death or on the transfer of property from the revocable trust to a U.S. estate tax protected spousal trust, the property is transferred because of the terms of the U.S. revocable living trust, not as a consequence of your death. As a result, the U.S. estate tax protected trust will not qualify as a testamentary spousal trust under Canadian tax rules. This means the U.S. estate tax protected spousal trust will be subject to the 21-year deemed disposition rules on the 21st anniversary of the trust's existence, which is based on the date the U.S. revocable living trust was created, not the date the U.S. estate tax protected spousal trust was created.

2) For more information regarding the use of a testamentary spousal trust in Canadian estate planning, please ask your RBC advisor for a separate article on that topic.

> Due to differences in Canadian and U.S. income and transfer tax laws, more often than not, a U.S. revocable living trust can be problematic for Canadian residents, including those who are U.S. persons living in Canada.

The estate planning will only work for both Canadian and U.S. tax purposes if the property is held directly by the deceased and not through a U.S. revocable living trust.

Canadian resident residual beneficiary

You may be the residual beneficiary of a U.S. revocable living trust set up by someone else. As a Canadian resident, there are potential tax implications that may arise due to differences in Canadian and U.S. tax laws. For U.S. tax purposes, the ACB of the property in a U.S. revocable living trust receives a bump up to FMV upon the death of the grantor. If there's a subsequent disposition of the property, the U.S. income tax (if applicable) is based on the gains that accrue on the property from the date of the grantor's death.

The Canadian tax treatment is different. Whether the U.S. revocable living trust is resident in Canada or resident in the U.S., the ACB of the property for Canadian tax purposes does not receive a bump up to FMV upon the grantor's death. Therefore, if the property is transferred from the trust to a Canadian resident residual beneficiary, the beneficiary receives the property at the trust's original ACB (i.e. without a bump up to FMV on the date of the grantor's death). Once the property is disposed of by the residual beneficiary, the beneficiary is subject to income tax on the gain on the property, including any gain that accrued up to the death of the grantor. Where the grantor paid U.S. estate tax on the value of the property on the date of their death and the Canadian residual beneficiary pays Canadian income tax on accrued gains, including gains that accrued before the grantor's death, double tax results.

This double tax issue also arises where the trust was resident in Canada, U.S. estate tax was paid on the death of the grantor, and the property is retained in the trust and later disposed of or deemed to be disposed of by the trust.

The double tax issue arises because there is no mechanism in the Canada/U.S. tax treaty for the residual beneficiary or the trust to claim a foreign tax credit for U.S. estate tax that was incurred by the grantor.

If you're a Canadian resident residual beneficiary of a U.S. revocable living trust that is not resident in Canada, the

following planning opportunities may be available when the grantor passes away to minimize the risk of double taxation:

- If distributions to a Canadian resident residual beneficiary are delayed until the year following the year trust property is sold, the distribution will be treated as a distribution of capital, which is not subject to Canadian taxation.
- If the Canadian resident residual beneficiary becomes the trustee of the trust, this results in the trust becoming a resident of Canada for tax purposes and results in a bump up of the ACB of the property in the trust to the FMV on the date the trust becomes resident in Canada.

Conclusion

Due to differences in Canadian and U.S. income and transfer tax laws, more often than not, a U.S. revocable living trust can be problematic for Canadian residents, including those who are U.S. persons living in Canada. Since they often result in double taxation, estate planning for Canadian residents generally would not include the use of U.S. revocable living trusts.

This article may contain strategies, not all of which will apply to your particular financial circumstances. The information in this article is not intended to provide legal, tax or insurance advice. To ensure that your own circumstances have been properly considered and that action is taken based on the latest information available, you should obtain professional advice from a qualified tax, legal and/or insurance advisor before acting on any of the information in this article.