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# Wills, Taxes and Estate Planning Law

Issues in Law You Need To Know

## Tax Obligations of U.S. Citizens Living in Canada

*It is the eve of April and Canadians are looking forward to warmer weather but, at the same time, feeling less than enthusiastic at the prospect of fulfilling their seasonal fiscal duty; that is preparing and filing their annual tax returns before the April 30th deadline. Similarly, American citizens, U.S. residents and U.S. green card holders also view April as “tax-season” and their deadline to file their tax returns with the IRS is April 15.*

Contrary to the Canadian tax system which is based on residency, the United States tax system is based on one’s citizenship as well as residence. Under the U.S. tax laws all U.S. Citizens regardless of their place of residence, U.S. residents or green card holders, have a statutory obligation to file their tax returns in the United States.

### FILING DEADLINES

U.S. citizens, U.S. residents and U.S. green card holders must report all of their worldwide income from all sources no later than April 15th of the year following

the taxation year. U.S. persons living outside the United States must also comply with the filing requirements but are granted an automatic two-month extension. Therefore, a U.S. citizen living in Canada must file his or her U.S. tax return by June 15th.

All U.S. citizens living in Canada must file their U.S. tax returns every year regardless of whether any taxes are due. Even if a U.S. person owes no tax in the United States, he or she should file a return, if only to preserve all available tax credits.

Failing to maintain filings may trigger unfortunate issues such as denying renewal of that person’s passport or delaying entry to the United States until that person’s tax record is updated.

### RRSPS, RIFFS & PENALTIES

RRSPs and RIFs are an area where there is a clear difference between the Canadian and U.S. reporting requirements.



Under U.S. tax law a U.S. citizen or resident owning a Canadian RRSP or RRIF must report any income and gain earned within his or her RRSP or RRIF on a yearly basis; not when the income is withdrawn as is the case under Canadian tax laws. To avoid double-taxation the Canada-U.S. Tax Treaty allows for an election in the U.S. citizen’s tax return to defer recognition of

the income earned and gains until such income or gain is withdrawn from the subject RRSP or RRIF.

However, to take advantage of that election the U.S. person must file his or her tax return on time and failure to do so may result in losing the right to make that and other similarly important elections.

### ESTATE AND GIFT TAX

Upon death, the United States levies a tax on the fair market value of the world-wide property of a U.S. citizen, U.S. residents or non-resident aliens if they own property in the United States. Consequently, any U.S. citizen living in Canada will be subject to the U.S. estate tax and ought to consider such in their estate planning (Canadians should consider the estate tax before acquiring U.S. property). There is a basic exemption available to U.S. citizens that may result in the estate being exempt from the estate tax but the prudent approach is always to seek professional advice on the subject.

One can see that, aside from the issue of estate tax, dealing with a deceased U.S. person's taxes upon their death can be a nightmare for estate trustees if the deceased failed to file his or her U.S. tax returns in previous years. This will inevitably result in an onerous

estate administration for the estate trustee and may have disastrous results for the beneficiaries. Also, an omission of the estate trustees to consider the U.S. estate tax and failure to ensure the deceased's tax record is in order may result in the estate trustee being personally liable for any taxes owed.

To avoid such dire consequences on death, U.S. persons must maintain orderly and up to date tax files.

### THE HIRE ACT

In light of the UBS banking scandal in the United States, Congress passed the Hiring Incentives to Restore Employment Act (HIRE). HIRE requires foreign banks and other financial institutions to report all U.S. persons' bank and financial accounts to the IRS. HIRE also provides that foreign entities such as corporations, partnerships and trusts must report U.S. persons' ownership or beneficial interests.

HIRE appears to provide over-reaching powers to the IRS since it essentially implements a system that "forces" the foreign financial institution or entity to submit to the IRS's jurisdiction. However, Canadian financial institutions and other entities will likely comply

with HIRE and report U.S. persons' bank and financial accounts to the IRS. This may complicate the U.S. persons' income tax filing requirements since their information will have to mirror the data submitted by the Canadian institutions or entities.

Although the impact of the HIRE exceeds the scope of this newsletter, those involved in Canada-U.S. dealings and taxes must be informed.

### RELINQUISHING U.S. CITIZENSHIP

Considering all of the onerous reporting obligations, the idea of simply relinquishing one's U.S. citizenship may seem tempting. However, to no one's surprise, the U.S. government has created onerous rules aimed at dissuading the relinquishment of U.S. citizenship for tax purposes.

To successfully relinquish your U.S. citizenship, one must first comply with all requirements of the U.S. State Department as well as completing and filing all required forms with the IRS; notably Form 8854 and ensure all tax returns are up to date.

Also, it is likely the U.S. person will be deemed to have disposed of all their worldwide assets at fair

market value and incur taxes on the deemed disposition; something to consider before starting the process.

It is also possible that taxes may still be owed after one relinquishes his or her U.S. citizenship. Those rules are complex and ought to be discussed with a tax professional.

The expatriate tax will also apply if the relinquishing person is present in the U.S. for more than 30 days in any calendar year during the 10 years following the date that person relinquished his or her citizenship. Note that the expatri-

ate tax only applies if it is greater than the amount of tax that would otherwise be imposed if you were taxed as a non-resident alien.

As one can clearly see, although tempting, relinquishing one's U.S. citizenship may not be worth the trouble involved.

### CONCLUSION

U.S. tax filing obligations are often misunderstood or simply ignored by U.S. citizens living in Canada. Ignoring or delaying the filing re-

quirements places one at tremendous risk. The consequences of being held liable for failure to file a tax return in the U.S. will result in additional taxes, penalties and interest to be paid as well as other unforeseeable consequences.

If you are a U.S. citizen living in Canada, we highly recommend you seek professional tax advice as to your U.S. tax duties and obligations and make every effort required to meet all deadlines for filings.

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### CALL TO THE BAR

Law Society of Upper Canada, 2007

### EDUCATIONAL BACKGROUND

- University of Ottawa, LL.L., 2007
- University of Ottawa, LL.B., 2005
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### PRACTICE SUMMARY:

Sébastien joined Tierney Stauffer LLP as an Associate in the Wills, Estates & Trusts Planning & Administrative Practice Group in 2009. His practise focuses on estate planning, will drafting and personal and corporate taxation. Sébastien has experience in resolving disputes with the Canada Revenue Agency (CRA), filing voluntary disclosures, assisting individuals with their tax related issues and tax planning for families and businesses. Sébastien is bilingual and practices in both official languages.

He has spoken at various seminars on estate, trust and tax matters. Sébastien has also appeared on radio and television discussing legal issues. He is a tutor for the Law Society of Upper Canada for the Estate Practice section.

Prior to joining Tierney Stauffer LLP, Sébastien practiced with another Ottawa law firm where he gained experience in tax law, charity law, estate planning and will drafting.