US estate tax planning for Canadians

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If you or your family members own US assets or are US persons[1], US federal transfer taxes (estate tax, gift tax, and generation-skipping transfer tax)[2] may apply. With planning, however, you may be able to arrange your affairs to pay less tax than without planning.

US transfer taxes may arise when assets are transferred to others during lifetime or upon death. For Canadians who are not US persons, US transfer taxes generally apply only to transfers of certain US assets, often referred to as "US situs property." Common types of US situs property include US real estate, US securities (held in both registered and non-registered accounts), and US business assets.

For Canadian residents that are also US persons, however, these taxes generally apply to transfers of most assets, wherever they are located.

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1 For purposes of the US federal transfer taxes, US persons are considered to be individuals who have US domicile, meaning that these individuals have indicated or demonstrated, in the view of the Internal Revenue Service, an intention to make the US their permanent home. US persons also include US citizens.

2 Transfer taxes may also be imposed by US states (in addition to federal transfer taxes) but are beyond the scope of this report.

Example

Suppose your worldwide estate includes a USD$5 million house in Florida and USD$45 million of Canadian assets, for a total estate of USD$50 million. Let's look at what would happen if the full estate value (after estate tax for each generation) passes from you, to your child, to your grandchild and finally to your great grandchild.

Estate tax

Estate tax applies to the value of assets upon death, at graduated rates that start at 18% and range up to 40% (for the part of the estate over USD$1 million) in 2025.

There is a unified credit that provides a lifetime estate and gift tax exemption, eliminating estate tax for US persons whose worldwide estate value is not more than USD$13.99 million in 2025.[3] US spouses may be fully exempt from the estate tax if the total value of the couple's estate does not exceed USD$27.98 million. For those who are not US persons and who reside in Canada, a prorated unified credit effectively exempts US situs assets from estate tax if the worldwide estate value is not more than USD$13.99 million.

The *Tax Cuts and Jobs Act* became effective on January 1, 2018 and effectively doubled the US estate tax exemption for deaths between 2018 through 2025. After that time, unless legislation is enacted, the estate tax will return to the pre-2018 regime and the exemption will be USD$5 million, indexed to inflation, or about USD$7 million in 2026.

Canadian residents who are not US persons

If you are not a US person, estate tax would only be payable on your USD$5 million Florida home. It's calculated as the estate tax on USD$5 million less a pro-rated unified credit. The credit is pro-rated using the ratio of US situs property (USD$5 million) to the value of the total estate (USD$50 million). Using the 2025 exemption of USD$13.99 million and estate tax rates, the potential estate tax bill would be USD$1.4 million[4]. If any of your beneficiaries are US persons, additional transfer taxes could arise when they pass away or gift the inherited assets, further eroding the value of the estate.

US persons

Figure 1 demonstrates the impact that estate taxes may have on wealth that is available for future generations if you, and your children and grandchildren are all US persons.

Figure 1: Tax on a USD$50 million estate over three generations, using 2025 estate tax rates and exemptions[5]

Family member	US estate tax (USD$)	Amount available to estate beneficiaries after estate tax (USD$)
You	14.4 million	35.6 million
Your child	8.6 million	27.0 million
Your grandchild	5.2 million	21.8 million
Total	**28.2 million**	**N/A**

3 The gift tax is integrated with the estate tax for purposes of this exemption. Any portion of the exemption that is used in connection with a lifetime gift would not be available again upon death. In this article, it is assumed that the individual has not made any lifetime gift, thus the entire exemption amount is available upon death. A discussion of the gift tax can be found further below.

4 It is assumed that the marital credit is not available.

5 The marital credit and any effects of inflation have not been considered.

Figure 1 shows that for your USD$50 million estate, the estate tax bill would be USD$14.4 million, leaving an after-tax estate of USD$35.6 million for your child. If your child has a USD$35.6 million estate, the estate tax bill would be USD$8.6 million, leaving an after-tax estate for your grandchild of USD$27.0 million. If your grandchild has a USD$27.0 million estate, the estate tax bill would be USD$5.2 million, leaving an after-tax estate of USD$21.8 million for your great grandchild.

In just 3 generations, over 56% of your USD$50 million estate would be payable as estate taxes and would not be available for future generations.

Gift tax and Generation Skipping Transfer (GST) tax

Canadians who are not US persons may be able to avoid estate tax on some US situs property simply by giving away the property prior to death.[6] Note that this does not apply to gifts of US real estate and other US tangible assets. But if you are a US person, you generally can't avoid estate tax simply by giving your assets away prior to death since there is a gift tax that is integrated with the estate tax. US persons must pay gift tax on the value of most gifts while those who are not US persons must pay gift tax on the value of gifts of certain types of US situs property, including US real estate.

Furthermore, if a US person makes a gift or leaves a bequest to an individual who is more than one generation younger, then GST tax equal to 40% of the value of the gift may be added to the estate or gift tax bill.

There are some exemptions from gift tax and GST tax. No gift tax applies for any gifts you make to your US-citizen spouse or, if your spouse is not a US citizen, for annual gifts of up to USD$190,000 (2025 amount). There is also an annual gift tax and GST tax exemption for total gifts up to USD$19,000 (2025 amount) that you make to any recipient. Finally, if you are a US person, there is also a gift tax and GST tax exemption of USD$13.99 million (2025 amount) for total gifts you make during your lifetime, which reduces the exemption that is available upon death.

Now may be a good time for US persons to take advantage of the current USD$13.99 million lifetime gift tax exemption. Using the current lifetime gift tax exemption could eliminate up to about USD$5.5 million of taxes that may apply after 2025. But remember, the gift has to make sense for you, taking into account all considerations, not only taxes.

Strategies to reduce the impact of transfer taxes

Given the high amounts involved, it may be worthwhile to explore strategies that may potentially reduce the impact of US transfer taxes. You should consult with tax and legal advisors in all relevant jurisdictions (including municipalities, provinces, territories, states, and countries), preferably prior to implementing any strategies. Be sure to consider current (and potential future) jurisdictions where the owners and potential recipients of assets reside, as well as where the assets are (or may be) located.

General strategies

Life insurance

Buying life insurance may provide funds to pay any estate tax liability arising at death. Note, however, that the insurance death benefit will increase the value of the worldwide estate, which may increase the amount of estate tax payable. When the insurance death benefit will be significant, consider holding the policy in a life insurance trust.

Consider making gifts during your lifetime

Consider giving away assets during your lifetime to decrease your worldwide estate value, which may reduce or eliminate the estate tax. If you are not a US person, you can also consider giving away US intangible assets, such as US stocks, during your lifetime to eliminate assets that would otherwise give rise to estate tax upon your death.

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[6] Although Canada does not have a gift tax, there could be tax on capital gains, attribution of income and gains, or other tax considerations.

When planning for gifts, consider taxes that could apply for gifts in the US and Canada (or other jurisdictions) and whether you may use any gift tax exemptions to shelter gifts from tax. And be aware that recipients of your gifts might also face taxes themselves when they later transfer their assets.

Gifting to both US persons and those who are not US persons

If you would like to gift your assets to family members, either during lifetime or upon death, consider transferring US situs assets to any family members who are US persons and non-US situs assets to non-US beneficiaries. The US persons will likely face US transfer taxes at a later date on any property they receive from you, irrespective of situs. On the other hand, US transfer taxes may not apply to family members who are not US persons if they receive only non-US situs assets from you.

Dynasty trusts

Rather than leaving your assets directly to US beneficiaries, it may be preferable to create what's often referred to as a "dynasty trust." While assets are held in a dynasty trust, they are not owned by the trust beneficiaries and, therefore, no transfer taxes apply in the hands of the beneficiaries.

To create a dynasty trust, you would transfer your assets, either during your lifetime or under your will, to a trustee who will manage the assets in accordance with the terms of the trust on behalf of the US beneficiaries. The trust's beneficiaries may include individuals who are not yet born (such as future descendants), or a class of beneficiaries (such as grandchildren). This permits flexibility to include future beneficiaries. Transferring assets to a trust during your lifetime may also help to mitigate probate fees that would apply to your estate upon death.

Gift tax and GST tax may apply for transfers of assets to a trust, so US persons should consider taking advantage of the current US$13.99 million lifetime tax exemption, as discussed previously.

More information on dynasty trusts is available in our report Heir un-apparent: Estate planning for US beneficiaries.

Strategies if you are not a US person

Choose investments that are not US situs property

Rather than investing directly in US securities, you may wish to invest in non-US investment funds (such as Canadian mutual funds, segregated funds or exchange-traded funds) that hold underlying investments in US securities.

Move physical/collectible assets from the US

US situs assets may include valuables (such as artwork, antiques, jewelry or vehicles) that you keep in the US The simplest way to avoid estate tax for these items is to physically move them out of the US.

Sell US situs assets during lifetime

US gift or estate taxes will not apply when you sell US situs assets, although you may pay tax on capital gains for appreciated assets that you sell. You can then use the proceeds to invest in assets that are not US situs (such as Canadian funds), to reduce or eliminate assets that attract estate tax when you pass away.

Non-recourse debt

US real estate may be financed using non-recourse debt, which is secured by the property and where the borrower is not personally liable if the proceeds of sale of the property is not sufficient to pay the debt. This can reduce the value of your US property for estate tax purposes. In practice, non-recourse debt may be difficult to source and is usually accompanied by higher mortgage interest rates.

Canadian corporation

Estate tax may not apply to property held in a Canadian corporation; however, a number of potential income tax issues (such as shareholder benefit issues and post-mortem planning concerns in Canada, and less favourable US tax rates on long-term capital gains), make this less attractive for US real estate. A Canadian corporation may be appropriate for holding other types of US situs assets, such as US individual securities.

Discretionary trust resident in Canada

A US vacation property may be acquired and owned by a discretionary trust that is resident in Canada. In a typical scenario, one spouse contributes funds to the trust and the non-contributing spouse (and sometimes their children) are named as beneficiaries. The beneficiaries may enjoy the vacation property without exposing it to the estate tax at their deaths and allow the contributing spouse to use the property as well.

Unlike a corporation, the trust can access favourable US tax rates on long-term capital gains. If the vacation property is still owned by the trust on its 21st anniversary, under Canadian tax law, accrued capital gains may be taxed in the trust for Canadian tax purposes at that time or the trustee may distribute the property to beneficiaries on a tax deferred basis. This is often a theoretical concern, as properties are often sold (upsized or downsized) prior to the 21st anniversary of the trust.

Conclusion

Advance planning may help to reduce transfer taxes, potentially leaving millions of dollars more for future generations to enjoy. US transfer taxes and the strategies that may be used to lessen their impact are complex. You should consult with tax and legal advisors, both in the US and any other jurisdictions where you or your family members (could) reside or have financial interests, prior to implementing any strategies.

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