



Dear Valued Clients,

Expiration of US Tax Breaks in 2011

Canadians, who own US-situs assets, could potentially face a significant US estate tax bill. The **2001** US amendments gradually increased the estate tax exemption and reduced the top estate tax rate over the past decade. In **2009**, the estate tax exemption was at an all-time high of US \$3.5 million and the top tax rate was 45 percent. Additionally, the **2001** amendments called for a repeal of the US estate tax for **2010**. However, the US estate tax system is scheduled on **January 1, 2011** to revert to what it was before the **2001** changes. Thus, after **2010** the top estate tax rate will be 55 percent and the exemption will be lowered back to US \$1 million for US citizens.

Reinstating the **pre-2001** rules will significantly increase the burden of estate tax. If a Canadian (or US) person died in **2009** with assets valued at less than US \$3.5 million, there was no federal estate tax on the estate, irrespective of the amount of US-situs property owned by the Canadian person. Even wealthier Canadians who died in **2009** owed little or no estate tax on their US-situs assets, due to the larger estate tax exemption. After **2010**, many more Americans would be exposed to the estate tax due to their ownership of residence, investments and other taxable assets.

As an example, assume that a Canadian bought US-situs assets for US\$300,000 in **2009** and his total assets (held worldwide) were US \$3 million that year – that is, his US-situs assets were 10 percent of his worldwide assets. In the event of his death in **2009** or **2010**, no US estate tax would be payable due to the larger estate tax exemption available to him in **2009** (i.e. US \$300,000 being 10 percent of the US \$3 million exemption) and repeal of US estate tax for **2010**. On the other hand, if the individual dies in **2011** and assuming the value of his US-situs assets remains unchanged, his estate would be entitled to only 10 percent of the US \$1 million exemption, or US \$100,000 – leaving \$200,000 exposed to US estate tax of approximately \$55,000. It should be noted that the US estate tax, in this case, would be payable even though there has been no appreciation in value of the US-situs assets. As well, pursuant to the Canadian deemed disposition rules which are triggered upon death of an individual, there could be a Canadian tax liability generated on death from fluctuation in value of US-situs assets due to foreign exchange differences.

Additionally, for those Canadians who are required to file US tax returns, there are also other tax reductions brought in under the previous Bush administration which are scheduled to expire on **January 1, 2011**. For example, for several years the top rate on both long-term capital gains and qualified dividends has been 15 percent. The top rate on long-term capital gains is scheduled to increase to 20 percent, and the top rate on dividends is scheduled to increase to the top rate on ordinary income, which itself increases from 35 to 39.6 percent. As a result, the combined corporate and shareholder taxes will be higher than in most industrialized nations, exceeding 60 percent.

Please feel free to contact us with your questions and comments.

Regards,

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