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## A Top Naples Realtor's Guide

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## The Canadian Florida Land Trust: The Most Versatile and Beneficial way for Canadian Citizens to hold Title to Real Estate in the State of Florida

### TITLE CONCERNS

Transferring funds to purchase a home or condominium is a simple process for Canadian buyers, however, many foreign buyers often overlook the consequences of their purchase. The acquisition of U.S. real estate by a Canadian citizens poses significant issues including but not limited to U.S. estate tax, capital gains tax, incapacity issues, complex Florida probate rules and creditor protection issues. Proper cross-border planning for Canadian Citizens must address all of these issues. A deep analysis is required to find the best solution. There is no simple answer or one size fits all. However, as a general rule, the vast majority of concerns can best be addressed by creating and taking title in a Canadian Florida Land Trust which is considerably more advantageous than owning property in a buyer's individual or corporate name or even a Canadian Trust.



## INTRODUCING THE FLORIDA LAND TRUST

This vehicle often referred to as an “Illinois Land Trust” because of its origin is a unique legal entity. This form of ownership is unfamiliar to most U.S. Lawyers and tax advisors due to the fact that Illinois and Florida are the only states that have a specific nearly identical land trust statute. This form of ownership is so far removed from classic trust law that calling it a trust can be misleading. The land trust is very versatile and differs from conventional trusts in many ways.

A land trust is a legal arrangement whereby the trustee holds legal title to the property, yet all ownership interest in the property lies with the beneficial owners of the trust. The trustee takes action, solely upon the direction of the beneficiaries. Among countless list of benefits to holding property in a Florida Land Trust is:

- The interest of the beneficiaries are not disclosed except upon choice, upon sale or upon order of the court.
- The beneficial interest is deemed personal property and avoids expensive and lengthy probate requirements.
- Provisions can be made in cases of disability which negate guardianship proceedings which otherwise may be required.
- It serves as a substitute for a will and provides planning providing direction for distributing the property upon death.

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- It can serve as a substitute for a partnership agreement and outline the various partners rights and interest in the property.
- Transferring interest within a land trust is simple and not subject to state imposed documentary transfer tax.
- In the event of sale, provided the property has been held for one year or longer, favorable individual capital gain rates of 15% apply rather than the regular corporate rate of 34%. In Florida there is further a state income tax for corporations, but not for individuals which can push the effective combined rate to 40%.
- When creating the land trust you can determine who will serve as trustee. Typically, in a Canadian Florida Land Trust this is the owner, though it does not need to be. Trustees serve a ministerial role as the beneficiaries direct the trustee on how they wish to manage the property. Trustees are the individuals whose name is made public and is the individual who signs deeds or mortgages at the direction of the beneficial owners. Successor Trustees can be listed and set forth in the event of death or incapacity of the initial trustee.



**Many of Our Canadian Clients Find This Guide Valuable in Helping Them With **Cross-Border Planning**, and Potential Issues With U.S. Estate Taxes, Capital Gains Taxes, and Complex Florida Probate Rules!**

## AVOID COMMON PITFALLS THROUGH A FLORIDA LAND TRUST.

In contrast, if title to real estate is placed in the buyers' individual names there are a host of issues to be concerned with:

### 1. PROBATE

Although a will, valid in Canada, will be recognized in Florida, unfortunately the will is not exempt from the costly and time consuming complicated probate process to transfer title in Florida. A Canadian Florida Land Trust can be created at the time of purchase and title can be placed in the name of the trust. Should the property owner pass away, provided title has been placed in the land trust, probate and related expenses will be avoided. Even though the property owner passed away, the land trust continues and the provisions within the trust set forth the order of the contingent beneficiaries (typically the surviving spouse and then the children).

### 2. INCAPACITY

Another advantage of Canadian Florida Land Trust is that it not only avoids probate and seeks to marginalize estate tax but it also acts as an excellent tool in the event of incapacity. If the property owner becomes incapacitated mentally or otherwise provisions are contained within the trust to provide for successor trustee(s) thereby avoiding the timely and costly process of Florida guardianship proceedings.

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## 3. CREDITOR PROTECTION

Unlike owning property in your individual name, the interest of the beneficiaries do not need to be made public in a Canadian Florida Land Trust. As a result, third party creditors cannot place a lien or seize the property as it remains confidential who the true owner is.

## 4. ESTATE TAX CONCERNS

Estate taxes are of paramount concern when Canadians own property in the U.S.

## 5. CREDITOR PROTECTION

Unlike owning property in your individual name, the interest of the beneficiaries do not need to be made public in a Canadian Florida Land Trust. As a result, third party creditors cannot place a lien or seize the property as it remains confidential who the true owner is.

## 6. ESTATE TAX CONCERNS

Estate taxes are of paramount concern when Canadians own property in the U.S.

- Unlike their U.S. counterparts, Canadians may only pass sixty thousand dollars (U.S) (\$60,000.00) tax free to their spouse or beneficiaries. If title is in a couples individual name, the surviving spouse may be hit with a significant estate tax that starts at 26% and climbs all the way to 45% based on the value of the estate. If properly drafted, shares within the land trust not need to be revealed until the time of death thereby making it possible to artfully manipulate the reported interest of the deceased and hopefully avoid estate tax.

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- Another tool to avoid or minimize estate tax is to make children beneficiaries at the time of purchase thereby increasing the number of \$60,000.00 exemptions by the number of individuals possessing an interest in the land trust. **There is no gift tax in Canada. If the funds are gifted to the children in Canada and transferred for closing there is no taxable event. However, if the property is located in the United States, a subsequent transfer of property to children will trigger a gift tax owed to the U.S.**
- Yet another technique to reduce exposure to the U.S. estate tax is to split interest ownership within the Land Trust. Under such an arrangement, an individual may acquire a life interest in the land trust share and his children could acquire the remainder interest in the property. Upon the death of the individual, there would be no estate tax on the life interest, since the life interest would have no value upon death. However one caveat: Should the children die while holding a remainder interest, the estate tax would be assessed on the value of the remainder interest. As a practical matter, children can obtain term life insurance at lower costs (due to their age) to protect them from estate tax exposure.

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## LESS FAVORABLE ALTERNATIVES

Other options to owning real estate individually is to take title in a Canadian corporation or to create a Canadian trust sometimes referred to as a Cross Border Trust. Below is an overview of both.

## OWNERSHIP BY A CANADIAN CORPORATION

In years past Canadian corporations were frequently used to own U.S. property. The corporation, if properly structured, was considered to eliminate U.S. estate tax on the death of the shareholder and the shareholder benefit issues did not arise due to an administrative provision of Canada Revenue. This type of corporation was referred to as a single purpose corporation. However, Canada Revenue withdrew this policy effective January 1, 2005. As a result a taxable shareholder benefit is created if the property held by a corporation was made available for the personal use of the shareholder.

The value of the taxable benefit is determined by either, the fair market rent approach or the imputed rent approach. Under the fair market rent approach the taxable benefit will be the fair market value rent for the property less any consideration paid by the shareholder to the corporation for the use of the property. Under the imputed rent approach, the taxable benefit is calculated by the greater of the cost and the fair market value of the property X the Canada Revenue Agency's prescribed interest rate, the operating costs related to the property paid by the corporation, less any consideration paid by the shareholders for the use of the property. As a result, it is no longer desirable to own property intended for personal use inside a Canadian corporation.

## OWNERSHIP BY A CANADIAN TRUST

A Canadian trust many times referred to as a “cross Border Trust” may also be used to own a U.S. property. If properly established, the trust may avoid any exposure to U.S. estate tax. In particular, the trust must be set up before the purchase of the U.S. property and the person who provides the funds to the trust for the purchase must not be a trustee or a beneficiary of the trust. The most common structure is where one spouse creates the trust (the grantor) while the other spouse and their children are named the beneficiaries of the trust. The grantor’s spouse and their children can then use the property rent-free during their lifetimes. The property held by the trust would not be included the grantor’s estate for U.S. estate tax purposes, nor will it be included in the spouse’s estate for U.S. estate tax purposes on his or her death.

Using a Canadian trust to own U.S. property does have its disadvantages. If the grantor’s spouse predeceases the grantor, the grantor must pay fair market value rent to the trust for the property to be excluded from his or her estate for U.S. estate tax purposes.

The only potential benefit that may result in creating a “Cross Border Canadian Trust” is that special wording may be put in the trust to preserve foreign credits in Canada under the Canada/U.S. tax treaty regarding capital gains tax. If properly structured, the seller may receive credit for the 15% United States I.R.S. Capital Gains Tax upon sale which otherwise would not be possible. However, in my opinion this potential benefit is pale in comparison to the potential estate tax which could otherwise be due if the wrong spouse dies first.

## **OTHER TAX CONSIDERATIONS TO BE AWARE OF...**

### **RENTAL INCOME**

Canadian snowbirds who rent out their Florida real estate are subject to a withholding tax of 30% of the gross amount of rental income. One way for Canadians to avoid the 30% gross withholding tax is to file a U.S. tax return and pay tax on the net rental income. The Canadian Citizen is then entitled to a refund for any taxes withheld to the extent the withholding amount exceeds to the tax which is payable.

### **TAXES UPON SALE**

Whenever a foreign citizen sells his or her interest in real estate in the United States it is a requirement to comply with FIRPTA (Foreign Investment Real Property Tax Act). At the time of sale 10% of the gross sale proceeds must be held in escrow until a determination can be made if a profit were realized upon sale. All of your initial acquisition costs together with any capital improvements are totaled to create your "basis". All expenses of sale are subtracted to determine your net proceeds. If your net proceeds are greater than your basis you will be taxed on the profit in the United States. This tax rate varies at the present rate of 15% if the property is individually held or held in a Land Trust to as high as 34% if held in the name of the corporation. In addition, there are further tax consideration upon the sale that could result in a double whammy when the profit is reported in Canada.

## GET IT RIGHT THE FIRST TIME

This means when purchasing property you need to title it correctly from the outset. If a decision is made to transfer the real property at a later date, Revenue Canada requires the value needs to be determined at the time of transfer to see if capital gain applies. Further, when a foreign investor transfers existing U.S. real estate by gift, he or she will be subject to U.S. gift tax. Again, this is the case even where an estate and gift tax treaty applies. There is no gift tax credit available to a transferor who is neither a citizen of nor resident in the United States (other than a limited annual exclusion of \$13,000.00).

Interestingly, a Land Trust will allow the gifting of shares up to \$13,000.00 annually so that it is possible to gift away your interest over an extended period of time utilizing a Land Trust. Otherwise, if gifted out right the gift tax of the fair market value would apply which is the same graduated rate that applies to estate tax.

At the end of the day, there may be unique facts and circumstances particular to your case that may warrant further investigation. As indicated above when it comes to proper planning there is no panacea or one size fits all, however, most common pitfalls can be avoided and countless benefits obtained by creating a Canadian Florida Land Trust at the time of purchasing property.

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## Canadian Florida Land Trust Assistance

Southwest Florida Real Estate Attorney Ronald S Webster is The Expert In The Creation and Implementation of a Canadian Florida Land Trust customized specifically For Your Unique Situation!

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