

Larry Jacobson



## Reporting Issues for US Tax Payers Residing in Canada

**T**he most common reporting required by a US citizen is their annual Income Tax Return, commonly referred to as a 1040.

This annual reporting is required, regardless of residency. The United States, contrary to Canada, taxes on **citizenship**, not **residency**.

For the most part, US tax payers in Canada will not owe any US taxes. First, there is a \$92,000 employment exemption; second, the Tax Treaty between our two countries allows for a Foreign Tax Credit. A US resident in Canada is taxed by the host country (Canada) first and then taxed by the United States.

Canada has a higher tax rate than the United States. The Foreign Tax Credit would in most cases negate any US taxes that are owed. Both countries subscribe to the theory that no one should be double-taxed on the same dollar. It is rare that a US person residing long term in Canada owes taxes in the United States.

The next annual reporting requirement is the Report of Foreign Banks and Financial Accounts (FBAR). This requirement is not new, but the United States has started to enforce the penalty provisions of noncompliance in reporting foreign bank accounts.

All foreign bank accounts of over \$10,000 must be reported. These accounts include RRSPs, RRIFs, RESPs, TFSAs, joint banking accounts, individual accounts, brokerage accounts, and possibly some life insurance accounts. Some may argue *how can they find me?*

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Under new foreign reporting rules, (FATCA Rules) Canadian financial institutions will be forced to disclose all their customers who are also US citizens. Further, the Tax Treaty allows the IRS to **require** the CRA to help them with enforcing US compliance issues.

The FBAR form requires the name and address of each account, the type of account, the account number, and the highest (maximum) value of the account during the calendar year.

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following:**

The IRS has just announced a new amnesty program that will remove the threat of fines if you do the following:

1. Write a letter to the US Department of the Treasury, enclosing the FBARs for the last 6 years.
2. File 3 years of income tax returns. If you owe less than USD\$1500 in US taxes in any one year, you will not be penalized. If any 1 of those 3 years is higher than USD\$1500, the amnesty will not be available.

The amnesty will cover about 90 percent of US expats. Americans in Canada should now start the process of becoming compliant. Although I don't prepare US returns, I can advise you on a strategy and recommend US tax preparers. Other issues that should not be overlooked:

1. The IRS treats Canadian RRSPs and RRIFs as *foreign trusts*. Filing a Form 8891 on your 1040 allows you to defer all income earned within the RRSP/RRIF until such time as you remove it.
2. Form 8891 does not cover the TFSA or an RESP; therefore, they are deemed to be *foreign trusts*, each year by December 31, all earnings are to reported. Our advice for US expats: Collapse and remove the TFSA and RESPs and, unfortunately, fund children's education in other ways.
3. Gift Tax: US tax payers who provide monetary gifts (to almost anyone) greater than \$13,000 in

any calendar year are taxed on the gift, and possibly up to 45% of the gift in excess of \$13,000. Like everything else in the US tax world, this issue is far from straightforward.

4. A US tax payer residing in Canada has to be concerned about the passive investment rule. Passive investments include too many investments to mention within this article, but two common ones are mutual funds (even those held in RRSPs) and shares in private companies. Many mutual funds are considered to be *foreign trusts* and, therefore, PFIC reporting is required each year. That could also apply to family holding companies that hold, say, real estate—again, a very complex area.

***A do nothing—wait and see strategy could potentially become a very expensive headache.***

Becoming compliant can be rather easy for many and very difficult and expensive for others. If you have clients who are Americans residing in Canada, they should start the process of becoming compliant sooner rather than later to take advantage of the Amnesty Program. A *do nothing—wait and see* strategy could potentially become a very expensive headache. ▲

*This article and the contents within should not be taken as US tax advice. One should always consult with a US tax expert regarding specific financial situations. The article and contents are the opinions of the author, not Macdonald Shymko & Company Ltd.*

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