

# Cross Border Issues Affecting Canadians Living in the USA

May 15, 2014

Ian Barclay, CPA/PFS

Jones Barclay Boston

303-592-4282

## A Discussion of the Financial and Tax Aspects (Canadian and US) for Former Residents of Canada Living in the USA

### 1. What is your Current Status?

- a. Residency Status- Canada or US
  - i. Canada- domicile (NR73 and NR74)
  - ii. US- Substantial Presence Test, Green Card
  - iii. Dual Residency & Tax Treaty
  - iv. State?

### 2. What Does Your Ideal World Look Like?

- a. Where would you like to spend your time?

3. A Proper Tax Analysis MUST look at the Canadian (and sometimes provincial), US (and most often State) consequences AND then see if the Canada-U.S. Tax Convention (Tax Treaty) applies

### 4. Canadian Savings, Pension and Compensation Plans- Company and Private (Alphabet Soup)

- a. **Canadian Tax-** 25% withholding (ITA section 212)
  - i. **Trick:** if payment is "Periodic" under Treaty- tax is 15%
  - ii. **Trick:** Draw down RRSP and minimize tax- file section 217 return. If withdrawal is between \$10-20k, you can get some or all of your withholding back. This works best for if little or no income other than pension income
  - iii. **Trick:** if your plan is "locked in" pursuant to Provincial Pension laws, as a non-resident you can un-lock the pension to access/withdrawal the funds.

#### b. US Tax- may have to pay tax annually on these.

- i. RPP- annuity with basis
- ii. RRSP (LIRA)- annuity with basis (Form 8891 annual reporting to defer income)
- iii. RRIF (LRIF)- annuity with basis
- iv. TFSA- contribute \$5,000 per year. Similar to Roth
- v. RESP- contribute up to \$50,000. Canada Education Savings Grants add 20%, up to annual \$500, lifetime limit \$78,200- DO NOT OPEN UP AN RESP while a US resident. Best to transfer ownership to Canadian resident, US Income tax on earnings must be paid annually  
**Trap: Need to file Form 3520 Annually (penalties 5% of assets, 35% income)**
- vi. DPSP
- vii. RCA- File Form 3520 annually
- viii. Stock Options

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- c. **Trick:** US doesn't tax the portion of pensions that result from non-deductible contributions made by the taxpayer. **Example:** since you do not get a *US tax deduction* for contributions to RRSPs, you have basis to the extent of these contributions, as well as any earnings and accretions occurring while a non-resident.

### 5. Government Retirement Plans

- a. **Canada-U.S. Social Security Agreement-** very important. Can help you qualify for benefits in both countries when you don't have requisite time
- b. **Canada**
  - i. **CPP (Canada Pension Plan)-** no CDN withholding tax (max 1,038.33/mo)  
**Trick:** taxed as US Social Security- max tax rate= 85%
  - ii. **CPP Qualification:**
  - iii. **OAS (Old Age Security)-** no CDN withholding tax, no claw back (.15 for each dollar over \$71,592). Max for 2014 is \$6,618.48
  - iv. **OAS Qualification-** Live 40 years in Canada between ages 18-65 for maximum benefit.
    - 1. **Trick:** If less than 20 years need to apply under the Canada-U.S. Social Security Agreement to qualify (*years in US count to qualify but not for benefit*)
- c. **U.S.**
  - i. **Social Security-** 2014 max benefit is \$2,642 per month
  - ii. **Social Security Qualification-** 40 quarters of earnings
    - 1. **Trick:** If less than 40 quarters, but have 6 actual quarters of earnings need to apply under the Canada-U.S. Social Security Agreement to qualify (*years in Canada count to qualify but not for benefit*)- *SSA 2490-BK Application for Benefits under a US International Social Security Agreement.*
- d. Can I receive CPP and Social Security?
  - i. YES- but **beware the WEP** (Windfall Elimination Provision). Many Social Security guides state the WEP reduces Social Security benefits if you had Canadian employment earnings and receive CPP. There is a strong argument that WEP should not apply to Canadian earnings. To help avoid this you might apply for Social Security using the *SSA 2490-BK Application for Benefits under a US International Social Security Agreement. This is processed at the Office of International Programs.*

### 6. Government Healthcare

- a. Qualification
  - i. Canada-Provincial- need to be in province 5-6 months to maintain
  - ii. U.S.- Medicare
    - 1. Qualification
      - a. 40 quarters of employment earnings, OR
      - b. Married to US resident or citizen who has contributed requisite for requisite earnings, OR

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- c. If 65 years or older and are a recent US citizen or green card holder (*or legal resident?*) and have constantly lived in the US for 5 years or longer, you can purchase Medicare. You can enroll in Part B (Doctors) without buying Part A (Hospital). But if you buy into A, you also must enroll in B. You can get Part D(Prescriptions) if you're enrolled in either A or B.

### 7. Owning Property in Canada

- a. Foreign Trusts- nightmare- Form 3520, 3520A
- b. Investments- brokerage accounts
  - i. US Reporting
  - ii. Canadian tax
  - iii. US tax- Foreign tax credit and Passive Foreign Investment Company (PFIC) issues
  - iv. Currency and fees
- c. Real Estate
  - i. Rental Income (25% gross or section 216 return, NR6)
  - ii. Sale of Property by Non-Resident of Canada
    - 1. Gain for Canada (subject to 25% of sales price unless file T2062 and T2062A to obtain Clearance Certificate to reduce with withholding)
    - 2. Gain for U.S. (step up under Treaty? Foreign Exchange)

### 8. Estate Planning

- a. What is an Estate?
- b. Residency
- c. US Estate Taxes (\$5,340,000 indexed)
  - i. Probate
  - ii. State estate taxes
  - iii. Tax is deferred on transfer to non-citizen spouse if QDOT
  - iv. If you receive more than \$100,000 from a foreign estate

### **YOU DO NOT NEED TO BECOME A US CITIZEN TO MINIMIZE YOUR US ESTATE TAX**

- d. Gift Taxes (\$14,000 and \$145,000)
  - i. Tax Reporting of Gifts from Canada- if aggregate value exceeds \$15,358 (Form 3520)
  - ii. **Trap:** Gifts by Canadian residents of US situs (e.g. stocks, real estate) property is subject to US gift taxes AND Canadian income tax.
  - iii. **Trap #2:** Gifts by Canadian residents of any sort of property are subject to Canadian income taxes. If the recipient is a US resident or becomes a US resident later the cost basis is the original basis of the grantor.
- e. Canadian Estate Taxes (no real estate taxes....but)
  - i. Deemed Disposition of Assets and Retirement Plans on death

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1. Deferral if passed to spouse
2. Probate Fees

## 9. Feeling Charitable?

- a. Want to donate to a Canadian charity and claim it on your US taxes?
  - i. Can deduct donation to Canadian university you or family attended
  - ii. Can deduct donations to Canadian charities, but deduction is generally limited to 50% of your Canadian sourced income (Treaty, article XXI)

## 10. Returning to Canada

- a. US tax status- Worldwide tax if citizen or Permanent Resident (green card holder)
  - i. Departure Tax Return- 1040C
  - ii. Retaining Permanent Residency
  - iii. Giving up Status
  - iv. **Expatriation**
    1. Form 8854
    2. Heroes Earnings Assistance and Relief Act (HEART)
      - a. Exit tax- over \$680,000 gains (2014)- can be deferred until asset sold- but NOT for pensions.
      - b. Inheritance tax for life on gifts to US residents >annual exclusion (\$14,000)
      - c. Applies to citizens and long term residents (lawful permanent resident in 8 or more of the last 15 years)
      - d. Applies on date citizenship is renounced or lawful permanent residency abandoned (Form I-407 with consular or immigration officer)
      - e. Imposed on “covered expatriates”
        - i. Average annual income tax liability over last 5 yrs >\$157,000 (2014)
        - ii. If your net worth is \$2M or more on the date of expatriation
        - iii. You fail to certify that you have complied with all US filings for prior 5 years
        - iv. There are exceptions for minors and dual –citizen for those born dual citizens.
    3. *Can I come back and visit the US?* If during the 10 year period after giving up citizenship or long term residency, you spend more than 30 days in the calendar year in the US, you will be considered a resident of the US for that year and taxed on your worldwide income. Exceptions: can be present for 60 days if you

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became a citizen or resident of a country in which you or your spouse or either parent was born.

- b. Canadian residency
- c. Deemed Acquisition of Assets upon becoming a Canadian Resident (NR74)
- d. Canadian healthcare- possible waiting period
- e. Social Security- can collect even if living in Canada
- f. Medicare- can collect even if living in Canada
- g. US pensions
  - i. Qualified Plans
  - ii. IRAs
  - iii. Roth IRAs- **Trick**: Considered pensions under Treaty and no tax paid in US and Canada upon withdrawal (after 5 years)
- h. US investments
- i. US Estate taxes- consider whether you retain living trusts.
- j. **Trap**: Beware Canadian Foreign Reporting Rules- Form 1135

### 11. FAQs

- a. I am on a temporary work visa. Should I apply for a Green Card (permanent residence status)?
- b. I have a Green Card. Should I become a U.S. citizen (naturalize)?
- c. Where should I retire?
- d. What should I do with my RRSP?
  - i. Should I collapse my RRSP and bring it to the U.S.
  - ii. It is locked in (LIRA, LIRF). Can I move it to the U.S.
- e. Should I roll over my RPP (employer plan) into an RRSP?
- f. Can I roll by RRSP into an IRA?
- g. I pay Alimony to my former spouse in Canada. Is it deductible in the U.S.?
- h. Should I exchange my C\$ for US\$ now. I think the C\$ is going \_\_\_\_\_
- i. Should I exchange my US\$ for C\$ now. I think the US\$ is going \_\_\_\_\_
- j. The Canadian dollar is low. Will I lose money if I exchange it now?
- k. I haven't declared my RRSP account for US purposes. What should I do?
- l. Is my Canadian will valid in the U.S. (see a US tax attorney)?
- m. Is my US will valid in Canada (see a Canadian tax attorney)?

*Ian Barclay is a dual citizen of Canada and the USA. He was born and raised in Montreal and attended McGill University. Ian worked for Ernst and Young in Montreal before he moved to Denver to attend the Graduate Tax Program at the University of Denver. He then worked for Price Waterhouse in Denver and Toronto providing international tax and financial planning services to businesses and senior executives. Ian is a CPA and Personal Financial Specialist, and principal in the Denver based, Jones Barclay Boston. The Firm provides fee only comprehensive financial advisory, income and estate tax, investment and other wealth management services to ultra high net worth clients throughout Canada and the USA.*