Cross-Border Tax Planning and Considerations

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Disclaimer

The information contained herein is of a general nature and based on authorities that are subject to change. Applicable of the information to specific situations should be determined through consultation with your tax advisor.

The tax rates and amounts in the presentation is for 2018 tax year only and are based on Canadian and US Federal information only. Individual provinces should be considered additionally.

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Agenda

- Who Is Required to File
- Current Tax Rates
- US and Canadian Investments
- Capital Gains Tax
- US and Canadian Retirement Plans
- US and Canadian Social Security Benefits
- US and Canadian Gifting Considerations
- US Estate Tax Considerations
- US and Canadian Foreign Reporting Requirements

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Who Is Required to File - US

- US Citizen
  - Worldwide income is taxable in the US
  - File Form 1040
- US Tax Resident Alien
  - Worldwide income is taxable in the US
  - File Form 1040
  - Residency start date
    - Green card
    - Substantial presence test
- Non-Resident Alien
  - US source income is taxable in the US
  - Form 1040NR
- All US citizens and green card holders are required to file annually until expatriation

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Who is Required to File - Canada

- Taxpayers must file their own individual tax return
  - No joint filing available in Canada
- All Canadian residents are required to report worldwide income
- If a taxpayer ceases Canadian residency, the taxpayer will no longer be subject to Canadian tax on worldwide income
  - The taxpayer may be subject to Canadian departure tax when ceasing Canadian residency
- A non-resident of Canada will only be subject to Canadian tax on Canadian source income (e.g. Canadian rental income)

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Current Tax Rates

US

- Federal tax rates: 10%, 12%, 22%, 24%, 32%, 35%, 37%
- Top tax rate of 37% is reached when income is over $600,000 if married filing jointly or $500,000 if filing single

Canada

- Federal tax rates: 15%, 20.5%, 26%, 29%, 33%
- Top tax rate of 33% is achieved when taxable income is over $205,842
- Top combined tax rate (federal and BC tax) is 49.8%

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US Investments

- Municipal bonds
  - Interest from US municipal bonds are tax-free for US tax purposes but are taxable for Canadian tax purposes
  - Taxpayers should invest in bonds that result in the higher return and not make their investment decision based on the tax-free nature of the bonds
- Capital gain distributions
  - Capital gain distributions are treated as capital gains for US tax purposes but are considered dividends for Canadian tax purposes
    - Therefore US capital gain distributions do not receive the same treatment as capital gains and are not taxed at 50% of the marginal tax rate

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US Investments – Special Flow through Vehicles

- For US tax purposes, taxpayers who hold US Limited Liability Companies (LLC) and S-Corporations (S-Corp) are taxed on the income that is flowed through to the individual shareholders
- For Canadian tax purposes, US LLC and S-Corp are considered corporations. Taxpayer will only be taxed on the distributions received and are considered dividends
- A possible mismatch on the timing of income recognition, income tax paid and foreign tax credits which may result in double taxation of income
- To ensure same tax treatment in both Canada and the US, a partnership structure should be considered

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Canadian Investments

- Dividends from Canadian corporations
- Registered Education Savings Plan (“RESP”)
- Tax Free Savings Account (“TFSA”)
- Non-US Mutual Funds

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Canadian Investments

- Dividends from Canadian corporations
  - Taxed at a lower rate than interest income as taxpayers receive a dividend tax credit to reduce tax liability
- RESP and TFSA
  - Required to include income on US tax return although tax exempt in Canada
  - May be considered a foreign trust:
    - Form 3520, Annual Return to Report Transactions with Foreign Trusts
    - Form 3520-A, Annual Information Return of Foreign Trust with a US owner
- Non-US Mutual Funds
  - Likely considered a passive foreign income company ("PFIC")
  - Required to report taxable earnings from the PFIC on a current basis
  - Form 8621, Information Return by a Shareholder of a PFIC
  - US citizens and tax residents can hold mutual funds within a registered retirement savings plan ("RRSP")

Capital Gains Tax

- Capital gains arise from the sale of capital property
- For US tax purposes, a taxpayer pay tax on capital gains at different tax rates depending on how long the taxpayer has owned the asset
  - Short-term investments (held for one year or less) are taxed at the taxpayer's marginal tax rate
  - Tax owing on long-term investments (held for more than one year) is capped at 20%
  - Capital losses claimed are capped at $3,000
- For Canadian tax purposes, the taxpayer will only be taxed on 50% of the gains at the marginal tax rate.

Capital Gains Tax - Home Sale

- A principal residence is exempt from Canadian tax purposes
  - Although the gain from sale is tax exempt, the sale must still be reported on the tax return
- Up to $250,000 ($500,000 if filing a joint return with spouse) of the gain from the sale of a principal residence is tax-exempt for US tax purposes
- If the taxpayer's spouse is a US non-resident, the taxpayer can consider gifting the home to their non-resident spouse before sale

US Retirement Plans

- Withdrawal from IRA (traditional, rollover, SEP or SIMPLE) and 401(k)
  - 10% early withdrawal penalty if withdrawn before age 59 ½
  - 25% penalty if withdrawn from SIMPLE IRA within two years of starting participation
  - Withdrawals are mandatory beginning in the year you turn age 70 ½
  - If the withdrawal is a lump-sum payment, it will be taxed at the marginal tax rate
  - If the withdrawal is an annuity, it will be taxed at 15% per Canada-US tax treaty
- Income earned in a Roth IRA account is tax-free in the US but taxable in Canada
  - Roth IRA is not a "foreign retirement arrangement" and is therefore subject to rules that apply to custodial accounts
  - Election can be made in the first taxation year of Canadian residency for income tax deferral for each Roth IRA plan or account
  - Any contributions made during Canadian residency will void the election and all income earned after the election is no longer in effect will be taxable

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Canadian Retirement Plans

- Registered Retirement Savings Plan (RRSP)
  - Income deferred for US tax under the Canada-US Income Tax Convention
  - Contributions are not deductible for US tax purposes
  - RRSP withdrawals for US tax purposes
    - Principal of RRSP can be withdrawn tax-free
    - Only income earned within the RRSP account is taxable
  - RRSP withdrawal for Canadian tax purposes
    - Withdrawal is taxable at the taxpayer's marginal tax rate
    - If withdrawn when the taxpayer is no longer a Canadian resident, the withdrawal is taxed at 25% non-resident tax rate

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Canadian Retirement Plans

- Spousal RRSP
  - Can be used to reduce US estate if spouse is a non-resident of the US
  - Can be used for income splitting and to avoid attribution
    - RRSP withdrawals from spousal RRSP will be taxed on the spouse's tax return

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US and Canadian Social Security Benefits

- US and Canadian social security benefits received by taxpayers that are Canadian residents are not taxable in the United States based on US-Canada Tax Treaty
- If you cease Canadian residency and receive Canadian social security benefits while living in the US, the social security benefits are taxable in the US and not in Canada
- Canadian taxpayers who receive US social security benefits are taxed on 85% of the income at the taxpayer's marginal tax return in Canada

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US Gifting Considerations

- Gift Tax
  - Tax on the transfer of property by one individual to another while receiving nothing or less than full value in return
- Gift tax return requirements
  - If a US taxpayer gifts any property with a value greater than the annual gifting limit, the taxpayer is required to file a gift tax return
  - Gift tax is paid by the donor
- Annual Gift Tax Limit
  - $15,000
  - $152,000 for NRA spouse
- Filing a gift tax return to report amounts in excess of the annual gift tax limit will reduce a portion of the unified lifetime gift and estate tax exclusion amount

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US Gifting Considerations

- Non-taxable gifts:
  - Gifts in the amount below the annual exclusion
  - Tuition paid directly to a qualifying educational organization for an individual
  - Medical expenses paid to a care provider for an individual
  - Gifts to your spouse (if spouse is a US person)
  - Gifts to qualifying charities

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Canadian Gifting Considerations

- Taxation of Gifts
  - Deemed to have sold at fair market value and pay tax on the capital gain
- Gifts to spouse and minor children
  - Attribution rule apply to gifts to spouses and minor children
  - Spouses
    - Gifts to spouses can be transferred at cost basis
      - Income and capital gains from the property will attribute back to the person giving the gift
    - Option to elect out of spousal rollover rules and transfer property at fair market value
      - Accrued gains up will be reported by the taxpayer, spouse will report future gains
  - Children
    - Deemed to have sold at fair market value when property is transferred to minor children
    - Income from the property will attribute back to the person giving the gift until the child is 18 years old
    - Capital gains will be considered capital gains of the minor children when property is sold

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Estate Tax Considerations

- What is estate tax
  - Tax on the transfer of the estate of the deceased person
- Estate tax limit
  - 2018: US$11.2 million
- Who needs to file an estate tax return
  - Any US citizen whose estate is valued at greater than the estate tax limit is subject to estate tax on worldwide assets
  - US green card holders who are domiciled in the US are subject to US estate and gift tax on worldwide assets
    - Taxpayer can be a resident for income tax purposes but not domiciled in the US for estate and gift tax purposes (depending on each individual taxpayer's circumstances)
    - If the taxpayer is not domiciled in the US, the taxpayer is only taxed on US situs assets
  - Canadian residents who own US situs assets such as US real estate and stocks in US corporations

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US Foreign Reporting Requirements

- Form 114 (FBAR)
  - If the taxpayer holds, in aggregate, over US$10,000 in non-US financial accounts
  - Late filing penalty: US$10,000
- Form 8938, Statement of Foreign Financial Assets
  - If the taxpayer has non-US financial assets above the threshold (US$):

Filing Status	Taxpayers Living in the US		Taxpayers Living Outside the US	
	Last day of the Year	Any time during the year	Last day of the Year	Any time during the year
Unmarried	50,000	75,000	200,000	300,000
Married Filing Separately	50,000	75,000	200,000	300,000
Married Filing Jointly	100,000	150,000	400,000	600,000

  - Late filing penalty: US$10,000

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US Foreign Reporting Requirements

- Form 3520 and Form 3520A
  - If the taxpayer owns, contributes or receives a distribution from a foreign trust
  - Late filing penalty: US$10,000 per form
- Form 8621, Information Return by a Shareholder of a PFIC
  - If the taxpayer has an ownership interest in a PFIC (non-US mutual fund)
  - Penalty: suspension in the statute of limitations with respect to the taxpayer's tax return

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Canadian Foreign Reporting Requirements

- T1135, Foreign Income Verification Statement
  - Must be filed if:
    - Canadian resident that, at any time during the year, owns specific foreign property costing more than $100,000
  - Late filing penalty: $25/day up to $2500
- T1134, Information Return Relating to Foreign Affiliates
  - Must be filed if:
    - Canadian resident that, at any time during the year, owns at least 1% directly and combined with related parties 10% in a foreign company
  - Late filing penalty: $25/day up to $2500
- T1142, Information Return in Respect of Distributions From and Indebtedness to a Non-Resident Trust
  - Must be filed if:
    - Canadian resident received a distribution from a foreign trust or is indebted to a foreign trust
  - Late filing penalty: $25/day up to $2500

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Thank you!

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Appendix

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US Federal Tax Rates – 2018

Rate	Joint Return	Individual Return	Married Filing Separately	Head of Household
10%	$0-$19,050	$0-$9,525	$0-$9,525	$0-$13,600
12%	$19,051-$77,400	$9,526-$38,700	$9,526-$38,700	$13,601-$51,800
22%	$77,401-$165,000	$38,701-$82,500	$38,701-$82,500	$51,801-$82,500
24%	$165,001-$315,000	$82,501-$157,500	$82,501-$157,500	$82,501-$157,500
32%	$315,001-$400,000	$157,501-$200,000	$157,501-$200,000	$157,501-$200,000
35%	$400,001-600,000	$200,001-$500,000	$200,001-$300,000	$200,001-$500,000
37%	Over $600,000	Over $500,000	Over $300,000	Over $500,000

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Canada (BC) Tax Rates - 2018

Combined Federal & British Columbia Tax Brackets and Tax Rates

2018 Taxable Income	2018 Marginal Tax Rates				2017 Taxable Income	2017 Marginal Tax Rates			
	Other Income	Capital Gains	Canadian Dividends			Other Income	Capital Gains	Canadian Dividends	
			Eligible	Non-Eligible				Eligible	Non-Eligible
first $39,676	20.06%	10.03%	-6.84%	9.23%	first $38,898	20.06%	10.03%	-6.84%	8.61%
over $39,676 up to $46,605	22.70%	11.35%	-3.20%	12.30%	over $38,898 up to $45,916	22.70%	11.35%	-3.20%	11.70%
over $46,605 up to $79,353	28.20%	14.10%	4.39%	18.68%	over $45,916 up to $77,797	28.20%	14.10%	4.39%	18.13%
over $79,353 up to $91,107	31.00%	15.50%	8.25%	21.93%	over $77,797 up to $89,320	31.00%	15.50%	8.25%	21.41%
over $91,107 up to $93,208	32.79%	16.40%	10.72%	24.00%	over $89,320 up to $91,831	32.79%	16.40%	10.72%	23.50%
over $93,208 up to $110,630	38.29%	19.15%	18.31%	30.38%	over $91,831 up to $108,460	38.29%	19.15%	18.31%	29.94%
over $110,630 up to $144,489	40.70%	20.35%	21.64%	33.18%	over $108,460 up to $142,353	40.70%	20.35%	21.64%	32.76%
over $144,489 up to $150,000	43.70%	21.85%	25.78%	36.66%	over $142,353 up to $202,800	43.70%	21.85%	25.78%	36.27%
over $150,000 up to $205,842	45.80%	22.90%	28.68%	39.09%	over $202,800	47.70%	23.85%	31.30%	40.95%
over $205,842	49.80%	24.90%	34.20%	43.73%					

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