

Snowbirds & U.S. Tax

Executive summary

Politicians are constantly searching for new tax revenue. Not wanting to upset national residents and ultimately voters, officials often include non-voting, foreign owners of domestic property as a key component to increasing tax revenue.

Canadian Snowbirds who own real estate in the U.S. are prime candidates for paying increased taxes. Since the taxation rules are complicated and can change frequently, it is vital to stay informed and in-the-know.

What you need to know

In order to be exempt from filing IRS forms or a U.S. tax return, three conditions must be met:

1. You do not earn any U.S. source income (interest, dividends, capital gains, rent) AND
2. You are not physically present in the U.S. for more than 182 days AND
3. You score less than 183 on the Substantial Presence Test:

- To calculate your Substantial Presence score add together
 - Number of days spent in the U.S. in the current tax year
 - One-third of the days spent in the U.S. from the prior tax year
 - One-sixth of the days spent in the U.S. the year prior to that

- An example:
 - 2014: Days in U.S. = 140
 - 2013: Days in U.S. = 93
 - 2012: Days in U.S. = 120

Add together 140 (days spent in 2014)
 + 31 (1/3 of 93 days spent in 2013)
 + 20 (1/6 of 120 days spent in 2012)
 191 (Your Substantial Presence Score)

These calculations can be further complicated by the fact that the IRS follows the calendar year, and typically Snowbirds stay six to eight weeks in one year and then another eight weeks or more in January, February and March of the following year.

Additionally, it is important to understand the IRS' definition of 'day.' The IRS counts any time spent during a calendar day, as a full day. If, for example, you cross into the U.S. at 11:55 pm, and return ten minutes later at 12:05am, the IRS would consider this two full days since you spent time during two different calendar days, even though it was only ten minutes in total time!

- Also important to note that the IRS includes all of your visits to the U.S. throughout the year, not just your winter holiday. Daytrips for shopping or sporting events, for example, must also be included in your Substantial Presence calculations and determination of total days in the U.S.

If you frequently travel to and from the U.S, you may want to keep a small journal in your car where you can write down the date, time and occupants for each time you enter and exit the United States. Currently, a credible journal is sufficient proof for the IRS.

Point #1, above, is not as straight-forward as it sounds. If the income is 'rent', then IRS forms, and likely a 1040-NR, are necessary.

Interest income is 'zero-rated' for Canadians, so technically the income should be declared, but the tax rate is zero, so no U.S. tax is levied.

U.S. dividends are taxed at a flat rate of 15% for Canadians, and if the proper filings are made from your broker (either Canadian or U.S. based) to the company paying the dividends, then the 15% should be withheld, and no further declarations in the U.S. is required. This withholding should be verified and included on Canadian tax filings.

If the capital gain is the sale of the U.S. real estate, it is best to consult a Canadian-based U.S. tax expert before you contemplate selling to anticipate the necessary steps and filings to repatriate your capital back to Canada.

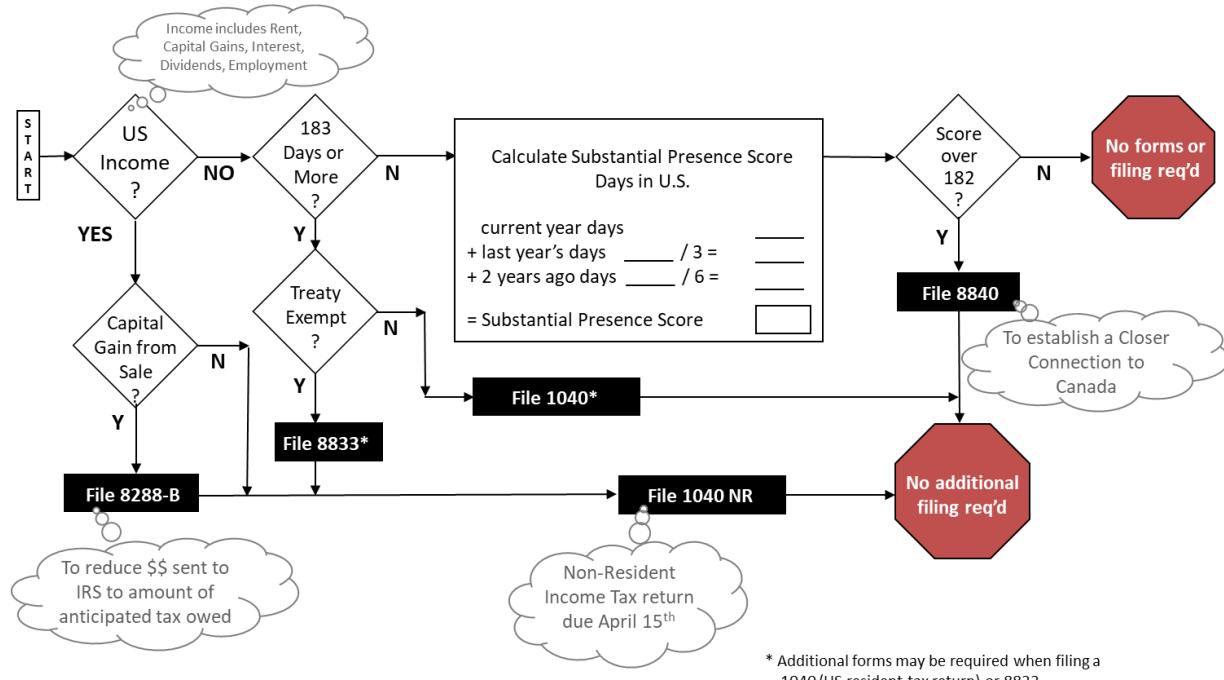
Further complicating the declaration of income is converting U.S. payments to Canadian dollars. The requirement is that the Bank of Canada exchange rate for the date of the transaction be used. If multiple payments occur, an average annual exchange rate is acceptable to CRA and can be found at <http://www.bankofcanada.ca/rates/exchange/annual-average-exchange-rates/>

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There is no need to travel to an IRS office as all documents can be found at www.irs.gov

Form #	What is it	When to use it
1040 NR	Non-Resident income tax	More than 182 days in US, or substantial presence has been calculated
1040 NR	Non-Resident income tax	If you have US source income like rent, interest or capital gains on sale of real estate
8840	Closer Connection	To avoid US tax filing when you have a substantial presence, but MUST be less than 183 days in US
8833	Treaty Exemption	In US more than 183 days, to avoid paying US tax, but must file 1040 NR simultaneously
8288-B	Withholding Certificate	To reduce withholding at sale of property from 10% to expected tax liability, even all the way to \$0
W-7	Tax ID No.	TIN is like a Canadian Social Insurance Number

Follow this flowchart to see if any forms should be completed by your clients and submitted to the IRS:



Some Key Factors to Know

- Canadians who earn U.S. source income subject to U.S. tax must file a U.S. tax return using IRS form 1040NR (non-resident)
- When U.S. property is sold by a foreign owner, the buyer is required by law to withhold ten percent of the purchase price and remit it to the IRS when the transaction is concluded (i.e. 'closed')
 - The buyer's lawyer when releasing funds withholds this money, because if it is overlooked, the IRS could require the buyer or the buyer's lawyer to remit the 10% while any tax implications are calculated
 - Filing a 8288-B can reduce this 10% withholding amount all the way down to the anticipated tax amount, even if the tax is zero
 - To file an 8288-B, a Tax Identification Number (TIN) like a U.S. Social Security Number or Canadian Social Insurance Number is needed
 - Obtaining a TIN requires 6 to 8 weeks, and must be in-hand prior to contract signing to facilitate the reduction of the 10% withholding
- If a Canadian stays in the U.S. for 183 days or more, he or she must file a full return or a non-resident return

If your Substantial Presence Score is 183 or higher, file an 8840 form to prove that you have a 'closer connection' to Canada, since any person can only have one official home country at any given time it is usually simplest for "Canadians" to be tax residents of Canada

The bottom line

If you are a Snowbird or travel abroad often or for extended periods, you should consider and know the tax implications of your travel plans. In the U.S. details change often. Staying in touch with your Advisor will help you understand these issues. Ultimately, an accountant with a specialty in cross-border tax will provide the advice you require tailored to your situation. Please contact us with any questions about the guidelines listed above.

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